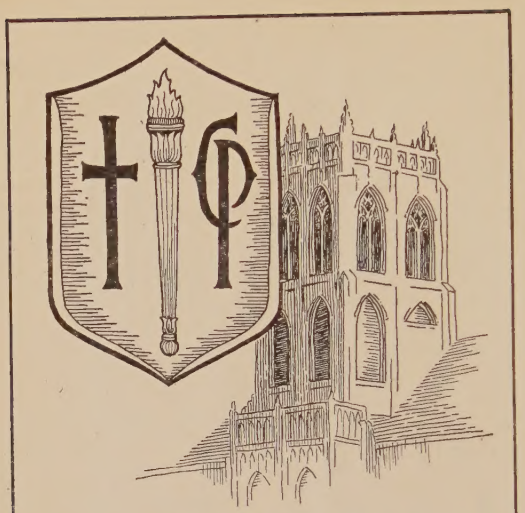
THE DAWES PLAN IN THE MAKING

Rufus C. Dawes



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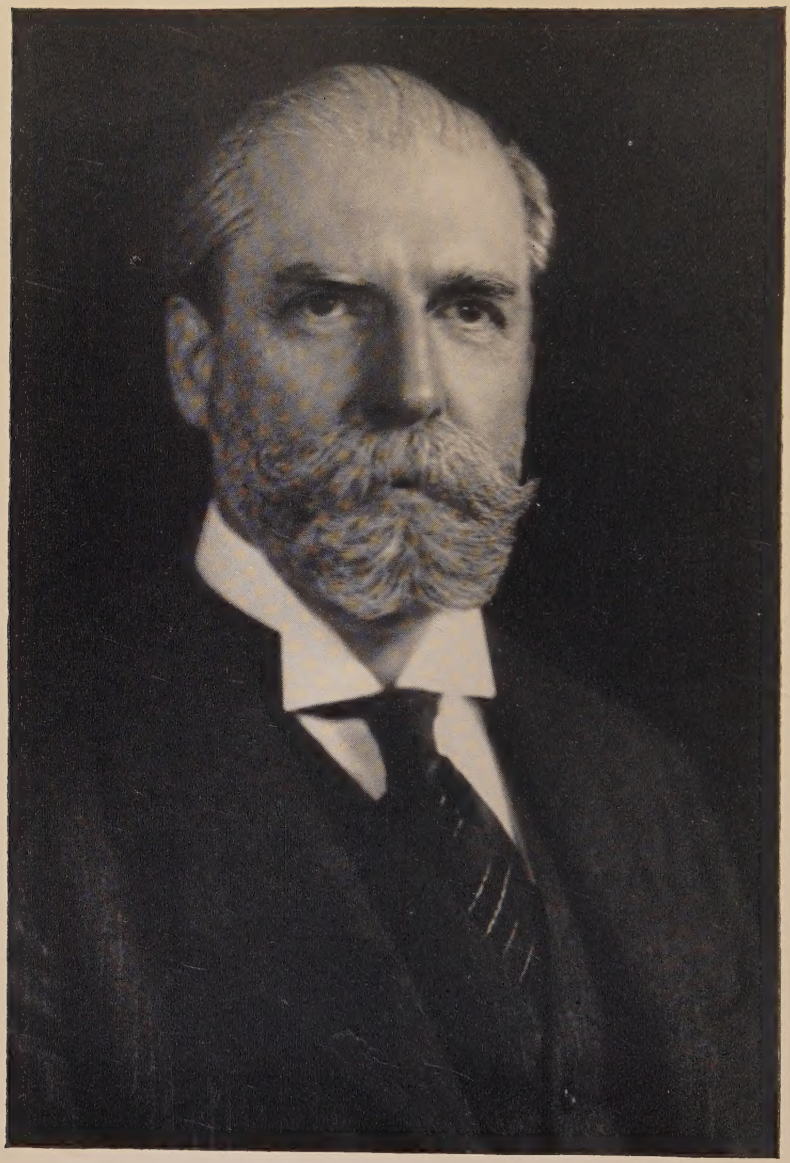
THE DAWES PLAN IN THE MAKING



CHARLES E. HUGHES
Secretary of State

College of the Pacific
Stockton, Calif.

THE DAWES PLAN IN THE MAKING

BY
RUFUS C. DAWES

WITH FOREWORD BY
FRANK O. LOWDEN

ILLUSTRATED

THE BOBBS-MERRILL COMPANY
INDIANAPOLIS PUBLISHERS

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Printed in the United States of America

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PRINTED AND BOUND
BY BRAUNWORTH & CO., INC.
BROOKLYN, NEW YORK

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FOREWORD

The appearance of this volume is an event in itself. It is now more than six years since the Armistice which ended the World War was signed. During that time countless books have been written upon the economic problems which resulted from the war. There is not only a prolific but a brilliant literature upon the general subject covering that period. The leading economists and publicists of the world have contributed to that literature. All of it, however, was more or less controversial, as was inevitable. It alternately criticized and praised the Treaty of Versailles. It justified or condemned the various conferences held from time to time to bring about a settlement of the reparation question. It was written largely from the standpoint of some one or other of the nations involved. The writers all agreed upon one thing and that was that the situation in Europe was desperate, if not hopeless. That this literature served a most useful purpose, however, no one can doubt. For every conceivable view was presented with unusual ability. Out of this extended and exhaustive discussion the facts of the situation began to stand out in a strong and clear light.

And now a volume appears, different from any of those which have preceded it. This book tells a story, not of divergent, but of converging national-

istic views. It does not tell of recriminations among the states of Europe, but of a sincere effort on the part of all to come again into friendly cooperation. It does not give the history of conferences worse than futile, but of one successful beyond the expectations of the most sanguine. Suspicion had given way to confidence.

This volume, written by Mr. Rufus C. Dawes, is the first extended discussion from an official source of the plan in its making. He was selected by General Dawes and Mr. Young to act as chief of the staff of eight economic experts who accompanied them from the United States to Paris. In this position he acted as liaison between the two American members of the Experts Committee and their staff of experts. It was his duty carefully to examine and in some cases brief the contemporaneous studies and comments of the experts as well as to advise the American members upon the economic problems involved.

No one could be in a better position than Mr. Dawes to write authoritatively on the economic principles involved in the plan and the machinery developed to make them effective.

Again, when Mr. Young was appointed First Agent for Reparation Payments in Germany, he selected Mr. Dawes for a place, during the installation of the plan, described by Commander Auld as "Allied Chargé-d' Affaires for Reparations"; when Mr. Young was absent he left Mr. Dawes in charge at Berlin, with full power of attorney. Here again he had a unique opportunity to become conversant

with the environment in which the plan was operating.

As to the ability of Mr. Dawes, the reader of this book will need no testimony of mine. He served upon the Commission to report upon the Pension Laws of Illinois and also as a member of the recent Constitutional Convention in Illinios, and has had a wide business experience, all of which has qualified him as a practical economist.

This book does not end on a note of pessimism for the future of Europe, but is serenely optimistic throughout. It is a clear, straightforward story told by an American business man of the achievement of practical men, thrown into the maelstrom of Europe, in an effort to accomplish that which the statesmen of Europe had for five years failed to accomplish, namely, economic peace. Being largely in diary form, it is therefore the gradual unfolding of the principles that finally found full expression in the report itself, and written with the full knowledge and understanding of an actual participant in this great achievement.

The years following the war were most distressing ones for all of Europe. No nation, save England alone, was able to balance its budget. The currencies of all the nations upon the continent were demoralized. The animosities of war, instead of abating when peace was declared, were actually increasing between some of the belligerents. Even among the Allies themselves differences and jealousies had sprung up. Europe was indeed in a most unhappy condition. To some it seemed an almost

hopeless condition. And all of this reacted inevitably on America and on the entire civilized world.

It was generally agreed that a sound and stable currency was the first thing required for a stabilized Europe. It was equally certain that a sound and stable currency was impossible until the several governments had found ways and means to live within their incomes. For no independent nation yet has been able long to indulge in expenditures beyond its actual receipts without inflating its currency. Disinterested observers had reached the almost unanimous opinion that neither of these things could be accomplished without a consideration of the vexatious reparation problem. Repeated and earnest efforts made by the governments involved had failed, and each failure naturally had aggravated the situation.

At this juncture, in December, 1923, the Reparation Commission decided to appoint a committee of experts to consider means of balancing the budgets of the nations involved and the measures to be taken to stabilize their currency. This was in response to a suggestion of Secretary Hughes in a notable speech which he had made a year before.

The American members of the committee thus created were General Charles G. Dawes and Mr. Owen D. Young.

When the Committee of Experts thus constituted unanimously agreed on their report, popularly known as the "Dawes Report" a new status quo in the economic peace of Europe and the world was created.

Their achievement illustrates well the important

part America may play in international affairs by simply furnishing leadership. We are the wealthiest nation on the globe. We are far enough removed from the other civilized powers to be free from the distracting influences which so often cloud their judgment and restrict their freedom of will.

Frank O. Lowden.

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THE DAWES PLAN IN THE MAKING

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CHAPTER I

THE EVOLUTION OF COMMITTEE OF EXPERTS—PERSONNEL OF COMMITTEE—ARRIVAL IN PARIS—PRELIMINARY CONFERENCES—OPENING SPEECHES—THE TREATY OF VERSAILLES — THE SCOPE OF INDEMNITY CHARGES — THE METHOD OF ASSESSMENT—THE SUGGESTION OF AMERICAN ECONOMISTS—ITS REJECTION AND POSSIBLE EXPLANATION—FIXING THE INDEMNITY—THE PROPOSALS OF VARIOUS GOVERNMENTS—THE CONTROVERSY AS TO BASIS OF CHARGES.

It was in December, 1922, that Secretary of State Hughes made his famous speech at New Haven in which he proposed that men of prestige, experience and honor be invited to consider the whole situation and report upon the amounts that really ought to be paid by way of reparations and upon a financial plan for working out such payments, and expressed the belief that without binding any of the nations or the Reparation Commission, such a report might and probably would correct many existing misconceptions and bring to the solution of these problems an enlightened public opinion. An account of the cor-

respondence and conferences which followed, and which eventually led up to the organization of the Committee of Experts has been prepared by Mr. Leon Fraser, one of the legal advisers of the Reparation Commission, and may be found in Appendix No. 1. The full text of the Commission's final decision is as follows:

"In order to consider in accordance with the provisions of Article 234 of the Treaty of Versailles, the resources and capacity of Germany, and after giving her representatives a just opportunity to be heard, the Reparation Commission decided to create two Committees of Experts belonging to the Allied and Associated countries. One of these Committees would be entrusted with considering the means of balancing the budget, and the measures to be taken to stabilize the currency. The other would consider the means of estimating the amount of exported capital and of bringing it back into Germany."

The United States, alone among the Allied Powers, not being a signatory to the Treaty of Versailles, had no official representative upon the Reparation Commission. It is represented by a so-called unofficial observer, that is, unofficial only in his relation to the Commission, for he is a very important official in his relation to the government at Washington. This difficult position is now held by Colonel James A. Logan, whose ability, tact and rare good judgment have enabled him to be of great service to his country without his ever having involved his government in difficulty. In the case of all the governments represented upon the Repara-

tion Commission, the names of those deemed worthy of serving upon these Expert Committees were given by the respective governments to the Reparation Commission, and invitations extended by the Commission to the men named. In this manner the following men were asked to serve: For Great Britain, Sir Robert M. Kindersley and Sir Josiah Stamp; for France, Monsieur Parmentier and Monsieur Allix; for Belgium, Baron Houtart and Monsieur Émile Francqui; and for Italy, Doctor Alberto Pirelli and Professor Federico Flora.

Of these, three, Sir Josiah Stamp, Monsieur Allix and Professor Flora, were eminent educators and writers on economic subjects; three, Sir Robert Kindersley, Monsieur Francqui and Doctor Pirelli, were prominent in banking and business circles in their respective countries; Baron Houtart was a man of long public career in Belgium, while Monsieur Parmentier was one of the most brilliant of the younger men in the French public service and a banker by profession.

In the case of the United States, the announcement was made from Washington that the government would view with approval an acceptance by private citizens of such an invitation from the Reparation Commission and also that Charles G. Dawes and Owen D. Young had been suggested as well qualified to serve upon the Committee, referred to as No. 1, for finding means for balancing the budget and stabilizing the currency. The Reparation Commission in extending their invitations designated Charles G. Dawes to serve also as Chair-

man of the Committee. Mr. Henry M. Robinson, of Los Angeles, was designated as the American member of the Committee to report upon the accumulation of German credits in foreign countries.

All of these men were educated as lawyers; all had practised this profession and all had abandoned it, Mr. Young to become Chairman of the Board of the General Electric Company and of the Radio Corporation of America, and Mr. Robinson and General Dawes to become bankers in Los Angeles and Chicago, respectively. Mr. Robinson had served as one of the advisers at the Peace Conference and also upon the Commission to consider the disposition of German ships. General Dawes had served in France during the war as Chairman of the Purchasing Board of the American Expeditionary Forces and as a member of the Inter-allied Committee of Supplies for the Allied Armies. Later he served, under President Harding, as the First Director of the United States Budget. All of these men served without salaries, but the Reparation Commission provided for their expenses. In the case of the American members, however, all of the expenses were assumed personally. A very early date was fixed for the first meeting of these Committees and little time allowed to make preparations and to gather a staff. General Dawes and Mr. Young had never met, though they had many friends in common.

Their first meeting was in Washington, December twenty-seventh, where they met to consult with Secretary Hughes and to pay their respects to the

President before their departure. Mr. Stuart M. Crocker, a confidential associate and friend of Mr. Young, came with him to this meeting, and General Dawes was accompanied by his brother, Rufus C. Dawes. Mr. Hughes made a long statement explaining the correspondence and conversations that led up to the appointment of these Committees, in which he displayed a great capacity for clear condensed statement. He believed that the restoration of productivity in Germany was a world necessity, so apparent as to force all nations to make at once the most earnest effort to effect a settlement. The nature of the inquiries submitted appeared to him to give an unlimited scope to the Committee's work, and to bring all the elements of the great problem under its consideration. He believed there was a great opportunity for the men on these Committees and a great hope for the world in their creation.

It was at this meeting that Rufus C. Dawes was designated as Chief of the Staff of Experts, and Stuart M. Crocker as Secretary. Mr. Young consulted with Secretary Hughes and with Secretary Hoover and with Mr. Dwight Morrow and Mr. Roland Boyden, former Unofficial Observer at the Reparation Commission, upon the selection of a staff of experts. Without there having been any previous discussion between them, they all recommended the same men. This greatly facilitated his task of selection. There was no hesitation upon the part of any of the men invited in accepting the appointment and their motives must have been to be of service, since in no case could compensation be of-

fered beyond a guarantee that they would in the end suffer no financial loss. To accept this service, they were obliged to cancel all engagements and to leave upon a moment's notice. The men thus selected were:

Joseph S. Davis, Professor of Economics at Leland Stanford University.

Edwin W. Kemmerer, Professor of Economics, Princeton University.

Colonel Alan G. Goldsmith, Chief of the Western European Division of the Department of Commerce.

Walter S. Tower, U. S. Commercial Agent at London.

Chester Lloyd Jones, U. S. Commercial Agent at Paris.

Charles E. Herring, U. S. Commercial Agent at Berlin.

Mr. Robinson brought with him Mr. John E. Barber, of the First National Bank of Los Angeles; and Colonel Leonard P. Ayres, now with the Cleveland Trust Company, formerly Chief of the Statistical Bureau of the American Army and one of the expert advisers to the American Commissioners for the Negotiation of the Peace in 1919; and also Mr. John B. Gundry, of Cleveland. This completed the organization of the Staff of Advisers.

On December 29, 1923, Mr. Young, General and Mrs. Dawes, Mr. Crocker, Mr. Rufus Dawes and his daughter, Jean, Mr. Tileston, who came as Mr. Young's personal stenographer, and Mr. Alan G. Goldsmith sailed from New York on the Steamer *America* of the United States Lines. Mr. Goldsmith

brought with him a trunk-load of documents and papers and was himself a walking encyclopedia of information. The Captain set aside the children's playroom for conferences, and daily conferences ensued. Mr. Young quickly won the admiration and deference of all. His well trained, orderly and agile mind, his long experience in the practise of the law and his familiarity with the management of great enterprises and with international negotiations in connection with them, all these, as well as an unusual patience, industry and instinct for method, qualify him to assume the lead in any discussion of this kind in whatsoever company he may find himself.

In the Treaty of Versailles, the Allied and Associated Governments affirm, and Germany accepts, the responsibility of Germany and her Allies for causing all the loss and damage resulting as a consequence of the war; but the Allied and Associated Governments recognized that the reserves of Germany were not adequate to make complete reparations for all such loss and damage. It was, therefore, required that Germany should undertake to make compensation for all damages done to the civilian population and their property during the period of the war, to make restitution for cash and property seized or sequestered, and to pay for all pensions and compensations in the nature of pensions awarded to naval and military victims of the war.

The Reparation Commission was constituted to determine the amount of the damage for which com-

pensation was to be required and to arrange for its collection. In limiting the power of this Commission, the more important provisions are to be found in Section 12, Annex 2, Part 8 of the Treaty. "In periodically estimating Germany's capacity to pay, the Commission shall examine the German system of taxation, first to the end that the sums for reparations which Germany is required to pay shall become a charge upon all her revenues prior to that for service or discharge of any domestic loan, and secondly, so as to satisfy itself that in general, the German scheme of taxation is fully as heavy proportionately as that of any of the powers represented on the Commission."

To facilitate the restoration of economic life of the Allied and Associated countries, the Commission was directed to take from Germany as security and acknowledgment of her debt, a first installment of gold bonds in the amount of twenty billion gold marks, payable, without interest, not later than in May, 1921, another issue of forty billion marks, bearing interest at 2½% between 1921 and 1926, and thereafter at 5%, and a further bond issue of forty billion marks to be issued when, but not until, the Commission is satisfied Germany can meet the interest, and the sinking fund obligations upon such bonds.

The framers of the Treaty, having laid down the scope of the damages to the repair of which reparation payments should be assigned, assumed, first, that at least sixty billion marks would ultimately be recoverable, second, that the damages were larger

OWEN D. YOUNG
United States Member First Committee of Experts

than this amount, and third, that the application of the rule of equality in the burden of taxation would probably result in the ultimate ability of Germany to pay more than the sixty billion marks, but the additional amount was exceedingly indefinite. Therefore, the Reparation Commission in subsequent paragraphs was given the authority to provide for further issues by way of acknowledgment and security, even beyond the aggregate of one hundred billion marks, but they were forbidden to require issuance of more than sixty billion marks until the interest and sinking fund on that amount were fully met. The Reparation Commission was also given authority to extend the date or modify the form of payments, but not to cancel any part of the indemnity fixed, except with the specific authority of all the several powers represented on the Commission.

During the Peace Conference, there were theories of methods other than the one adopted for fixing the payments to be demanded from Germany that were vigorously advocated.

The American Commission to negotiate peace had organized a Division of Economics and Statistics under the joint direction of Allyn A. Young, then a professor of Cornell University, and Colonel Leonard P. Ayres, then Chief of the Statistics Branch of the General Staff of the United States Army, and this Division submitted to this Commission, first a document prepared by Mr. Paul Cravath, developing the conclusion that Germany could pay about ten billion dollars in about twenty years, and expressing the opinion that the period of payments

ought to be restricted to about that time; and second, a "Memorandum on Germany's Transferable Assets." In this memorandum the argument was made that the German assets available for reparations were, first, such things as could be taken out of the country, as gold, ships, railroad rolling stock, cattle, coal, foreign securities, etc., and second, only the excess of exports over imports. The income from this latter source was computed to begin two years after the signing of the peace and to be at the rate of about five hundred million dollars or two billion gold marks annually.

The total payments provided for under this plan would have been about twelve billion dollars. It was intended to cover the actual cost of the restoration of property damaged in France, Belgium and Italy and the losses at sea. At that time, the value of property destroyed in France was computed to be about six billion dollars, with an outside possibility that it might reach ten billion dollars. This estimate seems to be confirmed by the experience of France in prosecuting her construction work, for up to the first of January, 1924, when it was officially estimated that the task was 62% complete, the expenditures, without interest, amounted to sixty-six billion francs, indicating a total cost of about one hundred billion francs for the completed reconstruction; and as the exchange value of the franc averaged about eight cents during the period of this reconstruction, the total actual expenditures for reconstruction will be the equivalent of about eight billion dollars.

When this "Memorandum on Germany's Transferable Assets" was submitted, it was found to be far below the demands made by the representatives of other countries, which were as high as sixty or even one hundred twenty billion dollars. It appeared in the discussions which followed that the American economists were the only ones who gave consideration to the principle that assets to be available for reparations must be transferable, and that transferable assets could be acquired by Germany for future payments only by exporting in the aggregate more than it was obliged to import.

The Division was then asked to revise its figures and to justify an estimate of a larger amount that might be collected, and a second memorandum was submitted, with a total of fifteen billion dollars named as the amount which might be received, but this addition was made by including the value of public works in former German colonies, and the ceded territories. The second memorandum suffered the same fate as the first, and the amount being so much smaller than the sums submitted by the representatives of other countries, they were requested to make a third effort. They succeeded by including items which would represent a loss to Germany, but no budget value to the recipients, in naming the sum of eighteen and one-half billion dollars, which was submitted, but with the warning on the part of some of the members of the Division that the figures had been "falsed" in the effort to increase the estimate.

The estimates of Germany's capacity to pay made

in Mr. Keynes' book, *The Economic Consequences of the Peace*, published several years later, followed closely the same methods and reached almost the same conclusions as the American Experts at the Peace Conference. It is regrettable that arguments and computations of the American experts did not produce a greater effect at that time, and it would appear that they were rejected not because of any error discovered, but because it seemed more just or more politic, or both, to base indemnities upon equality of tax burden rather than upon the limit of Germany's capacity to pay, and preferable to express the aggregate payable indefinitely. It is interesting to recall not only that the idea of fixing reparations upon capacity to pay was ably presented at that time, but that Germany's capacity to pay was measured as accurately then as it has ever been since. That it was a deliberate decision is to be inferred also from the statement of the German Government of May 29, 1919, from which the following is an extract:

"Germany is prepared to make the payments incumbent on her according to the program of Peace agreed upon, up to the maximum amount of a hundred milliard marks gold, namely twenty milliard marks gold up to May 1, 1926, the remaining eighty milliard marks gold afterward, by annual installments bearing no interest. The principle is acknowledged that these installments are to constitute a definite percentage of the revenues of the German Empire, and those of its federal states. The installment will come nearly up to the budget of former peace times. During the first ten years the install-

ments are not to exceed one milliard marks gold annually. The German taxpayer is to be burdened no less than the taxpayer of the most highly taxed state represented on the Reparation Commission. In conceding this, Germany acts upon the assumption that she will have to make no further sacrifices of territory beyond those mentioned and that she will again be granted freedom of action at home and abroad."

The Reparation Commission, in April, 1921, announced the London Schedule. It provided for the issue of:

"A" Bonds. Twelve billion gold marks to be delivered by July 1, 1921.

"B" Bonds. Thirty-eight billion gold marks to be delivered by November 1, 1921.

These to be issued and delivered to the creditors of Germany and to bear 5% interest and 1% for sinking fund.

"C" Bonds. Eighty-two billion marks to be issued only as and when the Commission is satisfied that the payments which Germany is able to make are sufficient to provide for the payment of interest and sinking fund on such bonds.

Annual payments demanded of Germany were set at two billion gold marks and 26% of the value of German exports. The bonds to be issued unconditionally and distributed to Germany's creditors were in the sum of fifty billion marks. Not more than eighty-two billion additional bonds were ever to be issued and none of these unless and until the payments of reparations collected from Germany from year to year were in amounts sufficient to pay in-

terest and sinking fund of the bonds issued and to be issued. Such a device could have no meaning whatever as a definite fixing of reparation, except as related to the method and effort of collecting annual payments, and the method enjoined upon the Commission was to establish the German scheme of taxation upon a basis fully as heavy proportionately as that of any of the powers represented on the Commission. The taxation endured by other nations seemed to them to be a satisfactory test of capacity to pay. Should a similar burden rest upon Germany, it was assumed the amounts to become collectible would carry and ultimately discharge fifty billion marks of bonds, and if more than necessary for this purpose could be collected, then additional bonds would be issued but never to exceed in the aggregate one hundred thirty-two billion marks.

The indemnity does not appear to have been fixed at one hundred thirty-two billion marks; rather it was an annual fixed payment, plus a variable annuity, determined by the principle of equality of taxation, and with the condition that the payment of such annuities should never exceed the present value of one hundred thirty-two billion marks.

At the Spa Conference, July, 1920, the division of reparation receipts among the Allies was fixed as follows: France 52%, Great Britain 22%, Italy 10%, Belgium 8%, Greece, Roumania and Jugo-Slavia together 6½% and Japan and Portugal each ¾%.

The difficulties connected with the collection of annual payments from Germany, whether in cash or in goods, required many conferences and created in-

creasing irritation, which culminated on January 11, 1923, in the invasion of the Ruhr by French and Belgian armed forces. During the latter part of 1922 and in January, 1923, there were many exchanges of views upon the general subject of an abatement of reparation demands.

France agreed to accept her proportion of A and B bonds already issued, that is 52% of fifty billion marks, and such additional sums as she would be required to pay on her inter-allied debts. England proposed a moratorium for four years, a payment of two billion gold marks annually for the next four years and two and one-half billion gold marks for the following two years, and after ten years, three and one-third billion gold marks, and the creation of a Foreign Finance Council to deal with such matters as the currency legislation, the budget and the General Treasury administration, and for the issuance of bonds; the obligation of Germany to be evidenced by bonds, the first series of fifty billion gold marks, 5% interest, but collection of interest to be suspended for four years and in consideration of which a second issue of bonds should be made in the sum of seventeen billion gold marks, at 5% interest. Accompanying this was a proposal for a partial cancellation of inter-allied debts.

This proposal was not acceptable to France, Belgium or Italy, and in the negotiations that followed, the proposition of England has seemed to be that to determine the capacity of Germany to pay is the first requirement for settlement since it would be

foolish to expect to get more than Germany can pay. France's position is that it is foolish to attempt to fix again, and particularly now, what a nation like Germany can pay over a period of fifty years. Each seems to think its statement conclusive and to resent the fact that it is not understood and accepted by the other. In his letter of August 11, 1923, Curzon says for England:

"It will not be contested that there can be no use in demanding from Germany more than she is capable of paying. What is the maximum she can pay, is a question of supreme importance to all her creditors. It is a question of establishing a fact, on the ascertainment of which any political arrangements or combinations for obtaining payment to the fullest extent possible must be based."

And Poincaré replies for France:

"The framers of the Peace Treaty rightly thought that a country's capacity to pay was essentially variable, that consequently a schedule of payments ought to be itself capable of modification, and that it would be for the Commission to take into account the economical fluctuations, to postpone the dates of payment when times were hard, and to advance them when the situation became more favorable. The idea of fixing once and for all Germany's capacity to pay never entered their heads. They could never believe that cosmopolitan financiers, however clever and experienced they might be, would be able to foresee the future and draw definite conclusions from uncertain and provisional data. They would undoubtedly have been still more amazed if they had been told that it was proposed to proceed to this fixing of payment at the time when Germany had

succeeded in arranging her own temporary bankruptcy, thus reducing for some time her capacity of payment to its lowest terms."

In May and June, 1923, the German Government proposed to fix the total of indemnities at thirty billion marks and suggested, as guarantees for the payment of this amount, (1) the detachment of the railway system of the Reich to be held in separate funds, obligations to be issued, having a first charge on its earnings in the sum of ten billion gold marks bearing 5% interest; (2) to secure the payment of a further annual amount of five hundred million marks by a direct mortgage on the entire business, industry, banking, trade and traffic and agriculture of the country, and all real estate; obligations to be issued on these in the form of a first mortgage in the sum of ten billion gold marks; and (3) a pledge of customs duties and imports and excise taxes on consumption of sugar, tobacco, beer, wine, etc., the annual return from which was estimated at eight hundred million marks.

These were some of the facts and conditions brought to our attention in our reading and conferences on board the boat. From our previous reading of newspaper comments and discussions, we realized that there seemed to be a general public conviction that indemnities had been fixed definitely at one hundred thirty-two billion marks and that the first duty of the Committee would be to recognize the impossibility of collecting any such sum and to fix upon some more reasonable amount as the basis of future adjustments. The gross burden of

indemnity charges laid on Germany, though more or less indefinite, nevertheless seemed to be a factor of the highest importance in connection with budgetary and currency adjustments.

But Mr. Young very early expressed the opinion that the approach to this question could not be made by reducing the aggregate charges against Germany to an amount within Germany's capacity to pay estimated at the present moment. It could never be made to appear just and equitable to give to Germany alone assurance that demands would never be made upon her to such an extent as to jeopardize her solvency, while other nations faced great difficulties and great uncertainties as well. He felt that France's ability to endure and survive was quite as much to be considered as Germany's capacity to pay, and that there was no advantage in saving Germany if her salvation is to mean the destruction of France. Some principle of justice and equity must be laid down as the basis of any settlement which the public opinion of the world could approve. There was no appealing principle to be invoked to support a policy of measuring the capacity of Germany to pay and then extorting payments up to that very limit. That might actually give to Germany a great advantage over her creditors which would offend a universal sense of justice, more especially by reason of the fact that in the industrial competition of the future, such an advantage might prove to be more and more damaging to her competitors. France, for instance, was certainly entitled to equality of opportunity in the international indus-

trial competition of the future, and in order to assure her and the other nations of this, there must be some adjustment upon a basis of approximate equality of the tax burden to be borne by all the nations. And he was of the opinion that if Germany were loaded with a burden no greater than her creditors, she could reestablish her power of production; and that the purchasing power of the world was increasing so rapidly that its markets would absorb the utmost production of Europe and America. But it seemed impractical to him to discuss the fixing of a definite charge against Germany on such a basis as to enable her to discharge it without bearing a burden of taxation equal to that of her competitors. And in his opinion it would be practically impossible, anyhow, to fix at this moment an amount certain to be within her capacity for future payments without that amount actually being far below her ultimate capacity.

The present difficulty of making payments was due to the low level of exports, which was only a temporary condition. Outside payment could be made only to the extent that there was a surplus of exports over imports. But a disordered currency and an unbalanced budget naturally checked production and reduced the exports. If these things were corrected, production would increase and with it capacity to pay and the capacity to pay could be measured only by future experience. One thing was certain, more would not be paid than could be paid. He emphasized the importance of establishing confidence and inspiring hope among the German

people. We all felt at the time that turning away from the discussion of the definite obligation to be fixed, and the measurement of capacity to pay based upon the exportable surplus, and substituting for it the principle of establishing equality in the burden of taxation, would be introducing a novel idea to which there might be some difficulty in converting others.

But when we arrived in Paris we found that others had reached the same conclusion by the same reasoning, and none of them spoke of it as being the rule of action laid down in the Treaty of Versailles. It must have been the case that all of the members of the Committee realized that a further discussion of the problem which had engaged the attention of the Reparation Commission and the premiers of the various countries for the preceding twelve months, would lead to no productive results unless some novel approach could be found. The members of the Committee would necessarily have to deal with exactly the information that had, for so long a time, been before the Reparation Commission, without any conclusion having been reached. Upon the contrary none of the inherent difficulties had grown less with continued discussion, but had rather become aggravated by pride of opinion and mutual misunderstandings. The agreement to approach the question by fixing a commensurate burden of taxation seemed to inject both the element of novelty and a defensible moral principle. At any rate the ready acquiescence of all of the members in this principle established, at the outset, a common veiw-

point and a mutual understanding which persisted throughout the entire conference.

At one of the conferences on the boat, General Dawes gave us the outline of what he might say at the opening meeting of the Committee. He will refer to the crisis in the Great War, which brought all the Allies to agreement upon the central command under Foch, after four years of uncoordinated warfare. He will maintain that it is the pressure of necessity alone that results in proper Allied coordination, and that if the Committee succeeds in devising a plan which is acceptable to the Reparation Commission and the Allies, it will be only because there now exists among the Allies a realization of the common calamity which can be avoided only by agreement upon a common and a commonsense plan. We all thought it excellent, and he will do it better on the day than he did it in the "dog kennel" as he calls the conference room.

Paris, Tuesday, January 8, 1924.

Disembarking at eight o'clock Monday morning, we left Cherbourg at twelve and reached Paris after six o'clock. All the newspaper men and many old friends of General Dawes were there. Colonel James A. Logan, the Unofficial Observer, was there and spent the evening with Mr. Young and General Dawes at the hotel. They discussed plans for avoiding misstatements by newspapermen, and for meeting so far as possible the necessity for getting out some sort of news, under the pressure of which these men work. They decided to issue only formal state-

ments, as far as possible. Colonel Logan is very astute and diplomatic and an excellent adviser.

Poincaré in supporting generally the national interest has the support of all parties. The Treaty must be upheld, the rights of France enforced, Germany must be brought to realize the necessity of complying with the terms of the Treaty, continuing payments and ceasing their passive resistance. Who could oppose such a policy? But his supporters are divided; some think every effort should be exerted to establish security and others think reparations must be the chief object of their efforts. Different policies are required to secure these respective objects. Then the Industrialists also form a strong group. When Poincaré turns from the general principle of protecting national interests to a particular policy, he will be opposed by one or more of these groups. The emphasis laid upon "capacity to pay" touches a sensitive nerve in Frenchmen now. They think it is the enemies of France who stress this question. The state of business, the falling franc, and the abyss into which it may continue to fall, creates apprehension that will make them anxious indeed for a settlement.

In the afternoon General Dawes and Mr. Young called in the newspaper men and handed them a statement to the effect that they came over with open minds and a sincere desire to be of service; that they had given no interviews and would give none except by formal statements and as to the conduct of the inquiry the only comment they had to make was one which would doubtless express the

feeling of all the members, to wit: that time was the essence of the value of this effort and the Committee ought to have continuous sessions.

General Dawes has made the first tentative draft of his address and took me with him and Colonel Logan this afternoon when he called upon Monsieur Barthou to consult as to what ought to be included and what omitted. Monsieur Barthou seemed to be quite satisfied with the proposed speech, but suggested that some reference ought to be made to Section 234 of the Treaty of Versailles. The General gave what at that moment appeared to me to be too ready assent. It had seemed to us that too much significance was attached to the mere willingness of France to permit a study to be made of this whole situation without limitation. When we came afterward to read carefully the procedure leading up to this conference, we found, for the first time, that the resolution providing for the Committee to investigate the problems of currency stabilization and budget balancing had a preamble to the effect that this action was taken by the authority conferred in Section 234. This section gives to the Reparation Commission the right to alter times of payment but not the aggregate amount of the total indemnity fixed. Perhaps Monsieur Barthou had it in mind that, with such a preamble, he could later claim that the inquiries of the Committee must be held within the same limitations as control the actions of the Reparation Commission. (See Appendix I—Terms of Reference.)

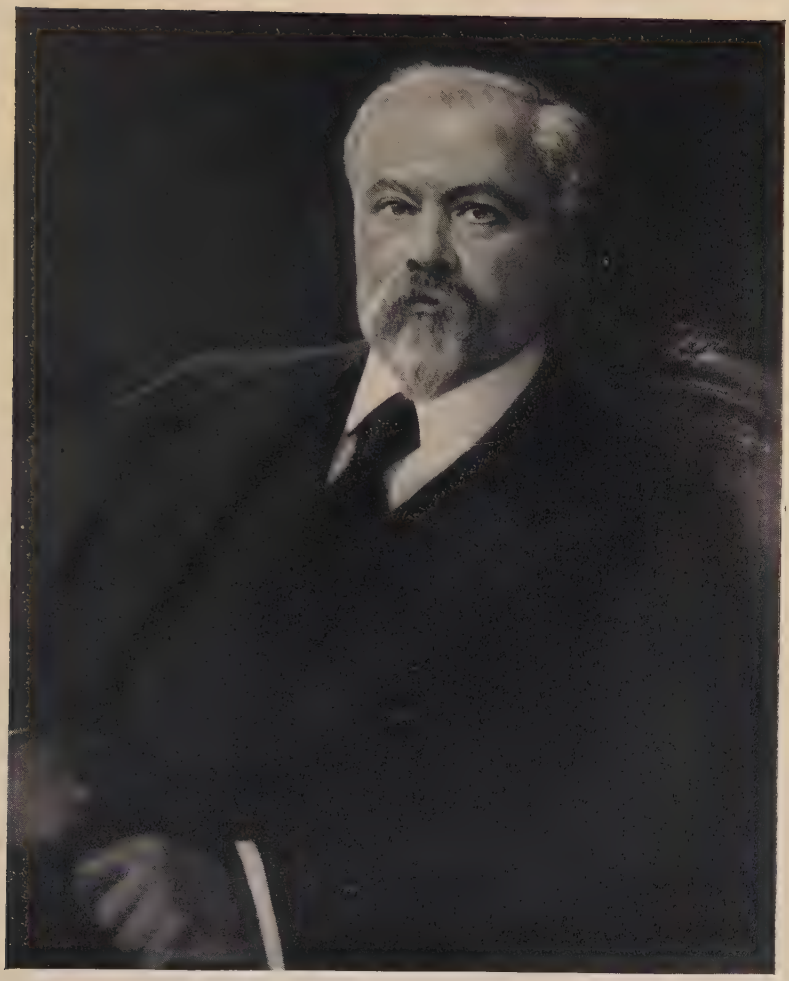
General Dawes was, therefore, right and very

wise to give immediate assent to Monsieur Barthou's request because he can comply with it merely by reading the preamble and the resolution by which the Committee was organized. To ignore the preamble after his attention was called to it would hardly seem defensible. The action of Sir Robert Kindersley, in stating that his acceptance of the invitation to serve upon the Committee was conditioned upon his understanding that the Committee had perfect freedom in making its inquiries, might have the same sort of motive behind it. The motive in both cases is probably precautionary. All parties to the conference seem to enter it in good faith, determined, if politically possible, to get results.

Tuesday, January 15, 1924.

Yesterday was the first meeting of the Committee. It was called in the Hall of the Reparation Commission, which was the dining-room of the Hotel Astoria, the very room to which it was reported that the Kaiser had invited his generals to join him at a triumphal dinner which he expected to give, at Paris, in the fall of 1914. It was a formal setting. Monsieur Barthou, President of the Reparation Commission, opened the meeting. He said:

"Gentlemen: The Reparation Commission, in welcoming you to your official functions, desires both to emphasize the importance of the task assigned to you and to thank you for having accepted it, some of you coming from so far, in a spirit of responsiveness and unselfishness which is universally appreciated.



Raymond Poincaré

"We do not expect of you the miracle of a sudden solution of the reparation problem, but we confidently hope that your competence, your experience and your authority will contribute to hasten the results to which our efforts are directed. The Treaty of Versailles is our charter, as it will be yours, and it is within the framework of that Treaty, under Article 234, that you will pursue your inquiry in full independence and with signal impartiality.

"The balancing of the budget and the stabilization of the currency which were closely connected, are the preliminary and essential conditions for the settling of reparation. We place at your disposal the reports drawn up by our inter-allied services and National Delegations, together with all documents you may require. You will be free to choose your own procedure. Under the Treaty, Germany is entitled to a just opportunity of being heard, and you will hear her representatives in the manner you may think most suitable. In the interest of all, we earnestly hope that her government and administrative services will facilitate your work, which is already so difficult and complex.

"Some solution must be found. It is not only Germany and her creditors who are interested in the reparation problem; it may be said without exaggeration that the peace of the whole world depends upon its settlement.

"Gentlemen, we ask you courageously to set to work, to produce the opinions which the Commission has unanimously demanded of you. Take your time, but let it be no longer than is necessary. We expect

much of you. The whole Commission rejoices that American citizens have come to cooperate with the Allied experts; this will greatly reenforce the authority of the Committee's findings.

"I ask General Dawes, on behalf of the Reparation Commission, to preside over your labors; his well-known competence and that energy which is known to legend, will help you to bring them to a speedy and successful conclusion."

General Dawes said:

"Gentlemen of the Reparation Commission and the Committee of Experts:—The difficulties involved in the determination of Allied policy, both in time of war and in time of peace, are little realized by the average citizen in all countries. To him, it seems strange that eventual common-sense agreements, which, in times of emergency characterize Allied policy, come about so slowly. He does not realize the barriers which must first be beaten down, erected by national pride and the pride and selfish interest of different Allied officials, whose powers are affected by any act of coercive inter-allied coordination and the incessant misrepresentations and intolerable interjections of those foul and carrion loving vultures—the nationalistic demagogues of all countries, who would exploit their pitiful personalities out of a common misfortune.

"Let me illustrate. Napoleon's sixty-fourth maxim of war was 'Nothing in war is more important than a central command—under one chief.' This great principle was realized and accepted at the beginning of the war by all the military authorities

of the world, and yet, after nearly four years of warfare, and the unnecessary loss of tens of thousands of lives and hundreds of millions in material wealth, the German Army, on March 21, 1918, struck at the junction of the British and French Armies and broke through because of the lack of a central command controlling the proper disposition of reserves. The British Army was forced back upon its own line of communications toward the channel ports and the French Army was forced back upon its own line of communications toward Paris and a gap was opened. Then it was that the Allies, facing the abyss, yielded a part of their sovereign power for the time being to the Central Command under Foch, which paved the way to Allied victory.

"What brought complete Allied cooperation in time of war? Nothing but overwhelming emergency. And when victory came and the Treaty of Versailles was signed, what again have we seen but those same natural forces and immutable laws of human nature which prevented an earlier agreement upon a central allied command in time of war, operating to prevent a common allied plan in time of peace.

"What is the question of to-day? Upon what does the success of this Committee depend? Upon power of persuasion? Primarily, no. Upon honesty and ability? Primarily, no. It depends chiefly upon whether, in the public mind and conscience of the Allies and of the world, there is an adequate conception of the great disaster which faces each Ally and Europe unless common sense is crowned King.

"Does this conception exist? We do not know, but we shall know. To this knowledge of whether this conception exists, the results of our work and the actions of the Reparation Commission thereon will perhaps be the final contribution. As an American citizen, invited to this place by the Reparation Commission, I can speak neither for the government of the United States nor for the American people, but as an individual, I can say that I have read, in shame and humiliation, the outpourings of the American nationalistic demagogues who undertake to lecture Europe in order to lift themselves into some petty office or maintain political popularity. Surely I have as much right as they to express my individual opinion of the attitude held by the great inarticulate mind and conscience of my people. Mr. Young and I will endeavor to express it in our actions upon this Committee. We come, humble in opinion, knowing that there is no barrier against the acquiring of knowledge like the pride of preconceived opinion. We come, knowing that you know much more about your own affairs than we do. We come, realizing the sacrifices which you have made for the victory to which our people also contributed, and of which we share the benefits. We know that thirteen hundred and eighty-five thousand of the flower of France's youth, nine hundred and forty-six thousand of Great Britain's youth, four hundred and sixty thousand of Italy's youth, forty thousand of Belgium's youth, and one hundred and twenty-seven thousand of Serbia's youth, together with the precious bodies of our own American youth, lie

buried close together here, across the sea. We know that from their sacrifice has come the great desire on the part of all peoples to make it worth while for their sakes, as well as for those who now live and are to live hereafter in the world.

"We come, only wanting to be helpful to you, who, with superior knowledge and longer experience, will take the initiative in the search for a common-sense agreement.

"We come, determined that nothing shall prevent our full usefulness if we have any, to you, in a work which is yours.

"In the last war, I was the Chief of Supply Procurement for the American Expeditionary Forces, under command of General Pershing. In the vanguard of our army I came with empty hands. Our great commander, General Pershing, at the date of our entry into the war, was faced with the necessity of building a line of communication and the other installations which would care for his eventual army. During the first seven months from the time we landed in France, there were shipped to us from America, only three hundred and fifty-seven thousand ship tons of supplies, and yet, when the American Army sailed back to the United States, it had required over seventeen million tons, of which ten million had been furnished chiefly by France and Great Britain, already stripped of resources by three years of devastating warfare. When we came, we stood empty-handed, reaching to our friends for needed supplies. You may be sure we did not start to tell our Allies what great men we were and how

much we knew. At their feet, humble in opinion, out of their larger experience, we tried to learn the lessons of war emergency. Great Britain furnished us ships to transport the bulk of our troops. We fired only French ammunition from French guns; our artillery was carried into action by French horses; we flew French aeroplanes; at the beginning it was the Belgian locomotives which carried our materials. Italy furnished us men to work upon our lines of communication. All of our Allies, from their depleted stocks, helped us with a generosity, to express gratification for which I find no adequate terms, but there was one supply in which our great government did not fail, and that was in the supply of two million splendid men, who, under General Pershing, marched and fought with your heroic troops in the final great and victorious struggle.

"With these memories of old associations, is it surprising that I feel as if I had come among friends? With the confidence and belief in each other which we had during the war and the love which has come from past associations in common difficulties; with the belief that, in the Providence of God, humanity is facing brighter days, and with the prayer that however little, as individuals, may be our contribution to better things, it will be all we have, let us approach our common work.

"Now let us consider for a minute the situation here as it is confronted by two American business men, who, some three weeks ago, were invited by the Reparation Commission to give it detailed attention in

connection with the proposed work which we start to-day. Like other citizens of our own and other countries, our information consisted of what we had read in the newspapers and gained from conversation with others presumably better informed. We had seen the Allies finally, really united under a single command, obtain a military victory which we had supposed was the precursor of a better world. For five years since that time and the signing of the Treaty of Versailles, we had seen the Allies losing the unity of understanding which is always essential to real peace and progress. We had come to know—in common with the citizens of all nations—that at last that lack of power to agree upon a common attitude and common action, had brought all Europe to a more critical and dangerous situation.

"Finding ourselves, then, as two American citizens thus suddenly called by the Reparation Commission, we devoted ourselves to making our own diagnosis of our environment with the advantage—if it may be called such—of access to expert information.

"This is no time to mince words. What to-day, at the inception of the work of this Committee, have we found? In the first place we see an impenetrable and colossal fog-bank of economic opinions, based upon premises of facts which have changed so rapidly as to have made the bulk of them worthless even if they were in agreement. With all due respect to the great ability of those experts who have wandered through this gloomy labyrinth, they could not have failed to come out in opposite directions. They

were confronted with the necessity of finding stable conclusions when no conditions were stable. If, in their computations, designed to clarify the mind, they dealt with the mark, the next week the mark was something else; if they dealt with the dollar, the pound, the French or Belgian franc or the Italian lira, there was one value in exchange for each and another in internal purchasing power; if they dealt with gold, there were values in pre-war gold and post-war gold to be considered. In general, we failed to find much value in economic arguments based on what ought to be instead of on what is—based, in other words on a constantly changing status quo.

"In the meantime, while these immense libraries, for they can be called by no other name, of legal arguments, of more or less obsolete statistics and of economic discussion, were being laboriously compiled for five years, the foundations of economic Germany have well-nigh crumbled and with them, the productivity of Germany. Again, as the world has seen the economic life of Germany ebbing away, the credit of all the European Allies has felt a preliminary shock, because the world realizes that if the German people lose their capacity to work, Germany loses the capacity to pay these reparations which are so great an element in European solvency.

"It would seem that the situation, as it has developed in the minds of your American members of this Committee, must have been regarded in much the same way by the Reparation Commission, to whom this Committee of practical men, free from

political pressure, owes its creation. Realizing that the house was afire, they proposed to find some water to put it out, without the further use of mathematics involving the fourth dimension.

"By their instructions, they enable us to start our work on the basis of a status quo. We are not asked to determine the legality of the occupation of the Ruhr; we are not asked to declare the political effects of this or that prospective act of common sense; we are not asked to give our opinion upon those things which politicians of all countries have interjected into a situation which primarily demands, for its proper consideration, business minds, uninfluenced by political ambition or thought of personal consequences. Upon our report to the Reparation Commission of a plan for the stabilization of Germany's currency and the balancing of the German budget, it is for them, not for us, to be concerned with political effects.

"The more I have talked with those here who are nearest the situation, the more do I realize the great wisdom which the Reparation Commission has shown in defining the purpose of our convocation: 'In order to consider, in accordance with the provisions of Article 234 of the Treaty of Versailles, the resources and capacity of Germany' we are 'entrusted with considering the means of balancing the budget and the measures to be taken to stabilize the currency.' If, without fear or favor, we suggest a plan for the stabilization of German currency and the balancing of the German budget, which the Reparation Commission deems fit to ratify, we will at

least have done this: we will have suggested that which has enabled the Reparation Commission to start Germany toward productivity; and the reestablishment of German productivity is the starting point of European prosperity.

"As the economic processes of Germany under a stable currency and with a balanced budget are revived, there will be demonstrated the capacity of Germany to pay. Basic and controlling facts will then first appear.

"Any common-sense individual can estimate the distance a well man can run. Fifty medical experts, gathered at the bedside of a dying patient, will give fifty different estimates of how far he can run if he gets well. The Reparation Commission and the world, upon the question of Germany's capacity to pay, have thus far been listening to the medical experts. Let us first help Germany to get well.

"Now that we are members of a Committee having a definite and authoritatively defined object in view, we are less concerned, for the moment, with the present capacity of Germany to pay, than with the present capacity and courage of this Committee to act.

"What is the use of deferring plain statement on this Committee? Why waste time in formalities and meaningless courtesies and conventionalities? Let us make, thus early, one practical suggestion:

"Under President Harding, I established the system of executive control set up by executive order under which the first budget of the United States was prepared, in accordance with our recent budget

legislation. I hesitate to call myself an expert on budget matters, lest I put my reputation for common sense under suspicion; but how could any one, expert or non-expert, suggest anything worth while about a German budget if the money collected through taxes and disbursed under the budget would not buy or pay for anything?

"The first step which we should take, it seems to me, is to devise a system for stabilizing Germany's currency, so that we can get some water to run through the budget mill. Let us build the mill after we find the stream to turn its wheels."

CHAPTER II

EARLY MEETINGS—POINTS OF AGREEMENT—ORGANIZATION BANKING AND BUDGET COMMITTEES—DOCTOR SCHACHT'S APPEARANCE AND ADDRESS—ANNOUNCEMENT OF BANKING PLAN AND BERLIN VISIT—EXPORTABLE SURPLUS—EQUALITY OF TAX BURDEN AND CREATION OF INTERNAL CREDIT—ITS PAYMENT ABROAD—ENGLISH BANK REPORTS—EFFECT OF INTERNATIONAL PAYMENTS ON COUNTRIES RECEIVING THEM—THE NECESSITIES OF FRANCE—ITS RECONSTRUCTION WORK IN RELATION TO REPARATION PAYMENTS—PROGRESS TOWARD AGREEMENTS.

Paris, January 15, 1924.

The Committee met again in the afternoon and proceeded at once to discuss the main features of its problem. There seemed to be no hesitation on the part of any of them in meeting squarely any question that was presented, and there was at the very outset a general acceptance of the opinion expressed by Mr. Young that as nearly as it could be determined, a debt service charge ought to rest upon the people of Germany, such as to produce a taxation burden equal, all things being considered, to the burden resting upon the other nations, both to satisfy a universal sense of justice and to tend toward establishing equality in the competitive industrial conditions of the future.

There was agreement also that the first task

to be undertaken was to discover the means to furnish a sound and stable currency and that this was very urgent; that the balancing of the budget would be comparatively easy, once stabilization be accomplished and that in the meantime it was important that the Rentenmark be sustained; that a new bank ought to be organized under the control of men to be selected outside of, as well as from within, Germany and that the chief function of this bank would be to issue its notes, secured by gold reserves, to be used as the circulating currency of Germany; that the capital for such a bank could be secured from subscription partly from citizens of other nations and partly from German Nationals, and that by this means there might be accomplished a recovery of capital belonging to Germans and now in foreign hands, or hidden within Germany; and that with a stabilized currency the budget could be readily balanced by means of an international loan of moderate amount.

Paris, January 21, 1924.

The reaction from the opening address seems excellent. Hundreds of newspaper clippings are laid on our desks and all comments are very favorable. Among public men and business men of France the feeling is that it gives great encouragement and hope as to the outcome of the conference. The English papers commend it and the reports are that it was well received in America.

Notwithstanding the inter-relationship of the two questions submitted and the early decision that they

must be treated as one, the Committee for the convenient distribution of the work organized a Bank Committee of which Mr. Young was made Chairman and a Budget Committee of which Sir Josiah Stamp was the Chairman.

Having learned that Doctor Schacht, the new President of the Reichsbank, was seeking capital in Holland and England, with fair prospects of success, for the organization of a new German bank of issue, the Committee invited him to Paris to explain from his view-point the conditions in Germany and his plans for the creation of a bank to provide currency. His first appearance before the Committee was on Saturday, January nineteenth. What he said to the Committee was imperfectly reported, but is so vital to an understanding of the problem that it seems advisable to include the gist of his address, though it is probably unfair to him, for his statement was of such a quality as to win the admiration of the Committee, and this report hardly does him justice.

He stated that when the United States entered the war, the dollar was quoted at six marks. Inflation continued during the war. Certain people believed that inflation was the only means of avoiding unemployment, but this was true only as long as the workers were deceived by the very high paper rates, for the real wages were in fact very low. When it became impossible to foresee the value which a sum received in the morning would have the following evening, inflation had to cease. This point was reached in July-August, 1923. The government

Sir Josiah C. Stamp
English Member First Committee of Experts

issued in August a so-called Gold Loan: five hundred million marks were offered and one hundred sixty-four million were sold. This loan had no real guarantees and some of the small denominations were still in circulation.

In addition large quantities of emergency currency had been issued, so-called "Notgeld" by all sorts of private and semi-private persons, chambers of commerce and corporations. Some of the persons and companies issuing "Notgeld" might possess foreign currency money as security, but there was no guaranty that this was the case. This "Notgeld" was circulating at its face value, based on paper marks. The Railway Administration which was now separated from the general budget, had been forced to issue paper marks. Unfortunately up till this time the Reichsbank had accepted "Notgeld" at its counters and every one printing "Notgeld" was increasing the circulation of paper marks. The Reichsbank had to accept this currency as no other was available, but this practise had ceased by the end of 1923.

The amount of currency in circulation in Germany before the war amounted to some six billion marks. Deducting even 10% for the territorial losses of the Reich, about five and four-tenths billions remain. Taking into consideration the fact that all prices in gold had increased by 70 or 80%, the sum actually available was insufficient.*

*Note:—The gold mark value of the strictly legal tender in circulation in Germany, exclusive of emergency money, as furnished by the German Government January, 1924, is shown in the following table:

Doctor Schacht had suggested a gold loan secured by real gold revenues which were to be procured by taxes payable in gold exchange, for example a 2½% turnover tax, on all commercial undertakings in foreign trade. As these transactions were carried on in terms of foreign currency, the taxes could easily be collected in foreign currencies and a real gold loan would have resulted, with gold income sufficient to meet interest payments. His suggested plan was not adopted.

A bank known as the Rentenbank was formed which was not in the true sense of the word a bank, but rather an Administrative office. Every property holder was charged with a mortgage of 4% on his total assets. In case of real property this charge was a first mortgage. Owners of movable property had to sign a bond stating that their assets were charged with an obligation of 4%. The total fixed and movable assets were upon the basis of 1912 valuation estimated to be of a value of eighty billion gold marks upon which 4% would be thirty-two hundred million gold marks. This mortgage was to be treated as security for the issuance of notes of the Rentenbank (known as Rentenmarks), which were

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IN MILLIONS

1913	6,670	February, 1923	513.8
1920	4,925.4	April, 1923	1,133.7
1921	4,350.1	May, 1923	761.2
June, 1922	2,723.2	August, 1923	607.6
July, 1922	1,730.0	December, 1923	496.6
Dec. 1922	716.5		

In January, 1924, the total gold mark value of circulating currencies in Germany, including the Rentenmark and other non-legal-tender money was about twenty-nine hundred million marks gold value.

the equivalent of the gold marks. The Rentenmarks issued by the Rentenbank were distributed as follows: eight hundred millions set aside as reserve; twelve hundred millions issued to Reich, (nine hundred at 6% interest and three hundred at no interest); and twelve hundred millions were to be issued to commerce, industry and agriculture at rates to be fixed later. The nine hundred millions issued to the Reich at 6% were intended to be used to cover the deficit up to April first. Of the twelve hundred millions set aside for commerce, industry and agriculture, he thought this might be soon exhausted as much credit was now required.

By the middle of November, inflation had proceeded so far that all calculations were made in gold. The government entered into the foreign exchange market but without altering the downward tendency—the dollar was then quoted at from three hundred eighty to four hundred twenty billion marks. Since the organization of the Rentenbank, the Reich had not borrowed from the Reichsbank. The total amount due from the government to the Reichsbank was one hundred ninety-one trillion marks. The three hundred million Rentenmarks issued to the Reich, without interest, were intended to redeem this sum. At the rate of three hundred eighty billion marks to the dollar, these three hundred million would not be sufficient, and Doctor Schacht had thought it right to raise the dollar quotation to something nearer the international parity ruling on other Bourses. In six days he brought up the dollar rate to four trillion two hun-

dred billion marks, and as 4.2 gold marks were worth one dollar, one billion (our trillion) paper marks were worth one gold mark and the relation between gold marks and paper marks was established. There were, therefore, the following currencies in circulation:

(1) The gold marks of the gold loan.
(2) The Rentenmarks.
(3) Paper marks at the rate of one trillion to the gold mark.

Of these the paper marks were legal tender.

German Nationals owned a certain amount of foreign currency, partly inside and partly outside of the country, which ought to be employed, if not in use now, for purchase of raw materials. The only way to secure these sums was by showing that they could be profitably employed. Confidence must be established. Doctor Schacht wished to establish a bank to acquire and use such funds, and upon such a basis as to gain the confidence of those who controlled them. He wished to establish the bank in Berlin and to have it connected in some way with the Reichsbank, though it would naturally have to be a separate organization. Its capital would be furnished by public subscription either in Germany or abroad, and he wished it to have foreign trustees, and would suggest the Swiss National Bank, through which German Nationals might subscribe to the stock of the bank without having their names published. Further capital might be paid in gold, or any foreign currencies on a gold basis. All such sums would be deposited with trustees outside of

Germany and would be employed in Germany either in opening credits or for issuing notes. The assets of the bank would consist of notes, gold, gold exchange and paid up deposits outside of Germany and neither the German nor any other government could touch them. Doctor Schacht was aware of the fact that the notes of such a bank would not be currency, since it would have no connection with the government. He did not see how a good government currency could be obtained unless the budget were balanced, the reparation problem solved, and a favorable balance of trade established, but money must be obtained immediately to meet the demands of commerce.

Doctor Schacht stated that his plan was not a permanent solution, but merely a scheme to restore confidence and to prepare the way in a few years to the return to a real gold basis. He naturally could have only an idea as to the amount of foreign currencies in the hands of German Nationals. The Swiss National Bank had informed him that in its opinion about one hundred fifty to two hundred million Swiss francs were held by German Nationals in Germany, and Mr. Vissering considered that about three hundred million Dutch florins were so held. Adding pounds sterling and dollars, Doctor Schacht thought some one billion gold marks of foreign notes were in the hands of German Nationals in Germany. The percentage of these sums which could be attracted by his proposal would naturally depend on the confidence with which it inspired the public. He hoped that some 60 to 80%

would be available. He thought that at first more would be forthcoming from outside Germany, and that later the notes in Germany would be attracted.

All the schemes that he had seen, such as the Hirsch plan, were on the same lines as his own, and did not provide for a permanent currency. He had seen no other schemes which proposed to set up a stable gold currency before the reparation question was settled. His scheme was generally accepted in Germany.

About two hundred million Rentenmarks sufficed to redeem the Reich's debt to the Reichsbank. It was easy to sell Rentenmarks for paper marks and to redeem the debt. The reason it had been possible to maintain stabilization was that the people were forced to sell foreign credits and currencies and owing to the reduction in the total purchasing power of paper marks, it was difficult to secure legal tender. The Rentenmark came into circulation late in November through payments to government employees and those of large companies. During the last few weeks large amounts of foreign credits had been sold, owing to the scarcity of currency and credit. This could not continue and credit for commerce must be secured, or stabilization could not be maintained. During the last few weeks the people had been in good temper and money values were secure, but production was halted. When all the Rentenmarks were used up, it would be necessary to give paper mark credits and invite the danger of fresh inflation and the fall of both the Rentenmark and the paper mark. Germany was in absolute need

of credit to buy raw material abroad. Figures for the last few months showed an excess of exports over imports. This probably indicated an inability to finance the purchase of imported raw materials and the exhaustion of her stocks. A fall in the value of the Rentenmark was to be expected.

Industry and commerce were in a deplorable condition. Only twelve hundred million Rentenmarks were available and paper credits could not be increased since that would destroy the value of the paper marks and Rentenmarks. Moreover the Rentenmark could not be used outside of Germany. Industry in Germany could make a fresh start with existing equipment but it lacked working capital. In agriculture there was danger that the farmers would not be able to sow. He wished with all his heart the Committee might discover a solution, but he also hoped that it would do nothing to interfere with his scheme, and would even afford it moral support.

January 23, 1924.

The condensed statement of the points of agreement existing between the members of the Committee at its meeting did not indicate by any means the scope of their discussion. In all essential matters they had outlined the same plan for the organization of a bank as was in the mind of Doctor Schacht, the chief differences being the wider scope of the Committee's plan and the matter of control, which of course was vital. Doctor Schacht appeared before the Committee again on Monday and was closely questioned in great detail as to all the conditions

and theories bearing upon the subject. At this time it appeared that he intended to proceed to organize a bank and that his conception of the urgency of the situation or his desire to have the bank in all respects according to his own plans might lead him to act without regard to the action of the Committee.

When this became known, there was presented a question to the members of the Committee—should they announce their plan for the organization of the bank or let Doctor Schacht announce it as his plan? If it were Schacht's plan, it might have less chance of success because of the lack of confidence abroad; or at least there would be more support abroad, of a plan announced by the Committee. Moreover, the Committee would secure great prestige at this particular time by announcing the plan as its own. This was done and the announcement appeared in the morning papers in the following words:

"The Committee have reached the opinion that an independent gold bank should be established in Germany, partly by mobilizing some part of the free reserves of gold and foreign currencies, which may exist in the hands of German Nationals, and which at present discharge no economic function, and partly by cooperation of foreign capital. In their view such a step will form part of the ultimate plan to secure future budget equilibrium and stable currency. In this connection, the Committee think that some of the features of the plan outlined before them by Doctor Schacht will prove, in due course, to be very useful, and they were glad to have the advantage of his views as a part of the whole field of possible or alternative action to be reviewed. The

President of the Committee, has, therefore, emphasized the need of allied unification in a program. The Committee are convinced that foreign cooperation in the management of such a bank is similarly desirable for ultimate success."

At the same time it was announced that the Committee would meet in Berlin on January thirtieth to consider the formulation of a definite plan. This incident served to bring the Committee to a decision promptly on an important matter and to put them in a position in which they must agree, and very quickly, on the details of the bank's organization. It promises well for the early completion of the work.

It was Mr. Young who suspected from some of Doctor Schacht's expressions that it was his intention to begin immediately the work of organizing the bank and who opened the discussion as to whether the Committee ought to sit by and let this be done. If Schacht could have organized his bank immediately on a solid basis, it would carry Germany over the crisis, which all seem to think is impending. Only to-day there appeared in the newspapers an interview with Luther, the Finance Minister of Germany, in which he is reported to have said that if Germany could not for a time at least be relieved of the payment of the cost of the army of occupation, it would fall so far behind in the revenues of the government as to bring about inevitably the fall of the Rentenmark. What can he mean except that it is the intention to inflate the Rentenmark whenever the shortage of government

revenues seems to demand it? Such items of news as this make one feel that it is a matter of supreme importance, involving the welfare of a nation and of the world and affecting also the comfort and even the lives of thousands of innocent people, that the new bank should be formed, and made to operate quickly so as to prevent the collapse of the Rentenmark.

Upon the other hand, can the new bank be established upon such a basis as to secure the confidence of the world if all control over its operations be left entirely to Germans? Will not the fear that the government would require an overissue of currency to meet the government's need for revenue, be felt abroad? It is almost as important to establish confidence outside of Germany in its ability to rebuild itself, as it is to reestablish faith and confidence among its own people. It is important also for this Committee to succeed and it can not afford to lose the initiative now. It is to be hoped that a way will be found to put into effect quickly whatever plan it forms.

Before leaving for Berlin the Committee had formulated its first tentative plan as follows:

SCHEME FOR THE CONSTITUTION OF THE GOLD BANK

(1) To establish German currency on a gold basis and to put an end to inflation.

(2) Paper marks would remain in circulation and for the moment no effort would be made to replace them entirely by notes of the new bank.

(3) The new bank controlling the note issue, the

ratio of the paper mark to the gold mark should be fixed at a trillion to one. The new bank to facilitate the liquidation of the Reichsbank by providing in exchange for the four hundred millions which represented its reserve notes of the bank. This liquidation would take place on behalf of the Reichsbank but under the control of the new bank, which would remit to the Reichsbank shares in the new bank to an amount equivalent to the excess of its assets.

(4) The liquid capital of the new bank should be at least four hundred million gold marks.

(5) This capital might be subscribed half in Germany and half abroad.

(6) The new bank could be entirely independent of all political power. Its Board of Directors should be composed half of Germans and half of foreigners; the Chairman should be a foreigner and have a casting vote.

(7) The new bank should alone have the privilege of issuing notes to the exclusion of the Reich, the states, the communes and any public or private personality. The bank would be forbidden to lend money to the state or to any of its administrative branches.

(8) The bank would be divided into two departments: the issue department whose seat should be abroad in a neutral country and the bank department whose seat should be in Germany. The issue department would be placed under the supervision of a Board of Controllers, instructed to insure that at no moment should any notes be issued in favor of any political power whatsoever.

(9) A state law should be passed laying down severe penalties for any controller who had failed in his duty as outlined above as well as any person who might have given false information to the controllers or persons delegated by them.

So far as our experts are concerned—meaning the

Staff of Experts—I think they would be glad to suggest some amendments, particularly to Section 8, providing for a division into a banking department and a department of issue. I think they would prefer some other adjustment to guard against the overissue of currency in order to meet the necessities of the fiscal balance.

The question as to whether it would be possible to stabilize the currency without balancing the budget emphazises immediately the necessity of a bank independent of government control and to be managed by business men, some from Germany and some from foreign countries. A government whose revenues are insufficient will issue more money, or if it controls a bank will have the bank issue more money. Assuming that a new currency be established and that the quantities of it emitted are just sufficient to meet the demands of commerce and establish a range of prices approximately the same as price levels in other countries, then to increase the volume of that currency merely to meet a deficit in the revenue of the government is to debase the value of money. It purchases less within the country than before. If it is exchangeable for any other form of money, gold for instance, it is exchanged and purchases are made outside the country and the poor money drives out the gold at home. If it is not exchangeable, it falls until like the late lamented mark, it has practically no value. This series of events will occur whenever too much currency is issued. Therefore, the control over the amount to be issued must be with the bank, which

Doctor H. Schacht
President Reichsbank

will issue it only as the demands of trade require it. The government would issue it chiefly to meet its own needs. When the government needs money, it ought to borrow it; it ought not to "make it." Banks should issue the notes on banking principles and in accordance with the requirements of business and without any regard to the financial necessities of the government for income. The government should meet its deficit, if such occur, by borrowing in the open market. In the case of Germany, the bank must not be in any way responsible for fiscal deficits and measures must be taken to safeguard its interests even if the government collapses. This is not likely to happen, for assuming a stable currency, there ought to be no difficulty in raising sufficient money to sustain the government, reparation payment for the moment being disregarded.

In considering the conditions under which the currency should be issued, it seems impossible to fix at the outset exactly what percentage of reserves to currency ought to be established, at least with precision, until more facts are developed, but Mr. Davis has pointed out that a large reserve in foreign credits may be accumulated by a new bank of issue, through its business transactions, in addition to the funds subscribed by the stockholders. For instance, the capital of the Austrian Bank was thirty million gold crowns, or three hundred eighty-five billion paper crowns. The note circulation at its first statement on January 7, 1923, was four thousand fifty-four billion paper crowns. The reserve was at this same date one thousand one hundred ninety-five billion

paper crowns or 29% of its circulation. This reserve consisted of approximately fifty billion paper crowns in gold, and one thousand one hundred forty-five billion paper crowns in foreign exchange of various kinds. The amount of capital was, even at this time—seven days after the bank was opened—less than one-third of the reserve in gold assets, but on November 7, 1923, the note circulation was six thousand four hundred ten billion paper crowns, 50% larger than on January seventh. The reserve had increased to three thousand four hundred eighty-one billion paper crowns or more than 50% of the circulation. The reserve at this time was nine times the capital.

There is also recognized the necessity of establishing a unified currency, and that in the future there should be one bank of issue, and only one, which should be given the power, and be charged with the duty of fixing a definite relative value to all the forms of currency that are to be kept in circulation.

These are some but by no means all of the important matters to be considered in organizing a bank of issue. Such a bank would deal through other banks very largely, in placing loans, receiving the guaranty of the bank through which the loan was placed, but at the same time have the right to enter into the so-called "open market" for money—thus to keep a certain control over interest rates and the flow of credit.

Such matters are recorded to give a general idea of how these discussions ramify. We do not have the advantage of attending the Committee's meet-

ings. It really is a Committee of Experts. Nearly all of its members have been making a deep study of these questions for five years. They have established mutual confidences and they are very rapidly approaching agreement on some of the important aspects of the problem. This agreement comprises in the most general manner the fixing of an equal tax burden as the basis of settlement, and the stabilization of the currency through a bank of issue. Assuming these conditions, there is to be anticipated a surplus of revenue beyond the actual needs of Germany for its own interior administration and this presents the problem of transferring this surplus into foreign payments or shipments upon reparation account.

Gold could not be shipped beyond the territorial limits of a nation without depleting that nation's supply, and the total quantities of gold in the world are less than the amounts involved in these international obligations. Money as represented by currency and credits, has its function as a medium of exchange and measure of values, only within the country itself. Paper francs and marks have no value in our country except in limited amounts to be used for the purchase of French or German goods. They can be useful only by exchanging them for foreign goods. The only method by which credits can be created in a foreign country, is, in the last analysis, by the delivery of goods or services in that country. If by taxation, an internal surplus in Germany were created, there would still remain the problem of transferring that surplus. Should

checks upon the account be made without regard to other conditions, these checks would have to be paid in gold or by the transfer of foreign credits, and both would soon be exhausted unless the supply of them were continuously increased; and they could be increased only by the exportation of goods. Enough goods must be exported, first, to provide the credit to buy from abroad such materials as are needed to support the population and, second, to supply the raw material for manufacturing the exportable goods; only the surplus remaining after meeting these demands can be transferred in the form of money or credits abroad, without exhausting the reserves of foreign credits and the domestic supply of gold and thereby depreciating domestic currency and lessening the power to make further purchases abroad of even the raw materials necessary to continued production. There must be a surplus of exports, visible and invisible, consisting of goods and services of every kind over the imports of every kind necessary to sustain life and support industry in any country, before that country can make investments or payments abroad. It is in the end this exportable surplus that measures the capacity of a country to make annual payments abroad.

It is the exportable surplus that makes payments possible. But what makes exportable surplus? It is in part that condition of affairs which makes men contented and ambitious and eager to throw themselves into organized work for production. To give to Germany a more definite statement of its obliga-

tions and some control over the time of making its payments ought in itself to help to produce this state of mind and feeling. There has been too much of a tendency to think of an exportable surplus as a fixed factor in the problem, whereas, it is itself as much a variable as any of the other factors. It depends upon purchasing power abroad as well as upon productive capacity at home, and settlement of reparations would increase both. If the settlement be such as to establish confidence and inspire hope and to call forth the energies always released by such feelings, productivity will be stimulated and the exportable surplus will increase. Determining capacity to pay is not the first step toward settlements; the discussion of it seems actually to have obstructed a settlement. It is more nearly correct to say that a settlement is the first step toward determining and developing the capacity to pay. But for months the general public discussion has been upon such topics as the capacity to pay measured by the exportable surplus.

To some extent Germany has been injured in recent months by being obliged to make payments and deliveries of goods that were greatly needed at home. Her capacity to pay at the present time has been thereby reduced. To be relieved for a time of such demands, and to permit the surplus of taxation proceeds over administrative expenses to accumulate, would enable her to build up her organization for production and grow in the ability to make payments later. On the other hand, such is the gloomy view taken of conditions in Germany by

some writers, that they seem to doubt if there would ever be a surplus of exports or an ability on the part of Germany to make exterior payments in any important sums, and some have even questioned its ability to raise by taxation sufficient sums to balance its own budget.

If such gloomy forebodings be true, then neither the method under discussion nor any other will ever extract important payments from Germany. The truth must, however, be determined by experience and not argument. The world would never be satisfied to accept a logical demonstration of incapacity to pay. But it has been so much impressed with the danger of extorting too much as to prefer some method that guards against this danger, without abandoning the effort to make further collections.

The important thing is to make some settlement to put an end to discord and dissension, to find some basis for the resumption of normal commerce, or in the words of Secretary Hughes to reestablish confidence. With confidence restored and business resumed, there would be set up at once a flow of capital to Germany. The exhaustion of working capital within Germany and the excess of such funds in the United States would quickly establish a margin in the interest rates which would act with the certainty of natural law to attract American capital to Germany, at first, perhaps, in short-time credits, but very soon in long-term bonds, the proceeds of which would have as much weight in fixing rates of exchange as credits transferred in payment for exports. The proceeds of such investments would

also increase the capacity of Germany to produce articles of export. The payment of interest upon such investments would, in the end, also require the shipment of goods out of Germany, but the period of time within which the capacity of that nation to produce could be developed, would be greatly extended. During the period of its greatest development the United States constantly increased its indebtedness to European countries. This indebtedness, expressed in the form of bonds on railroad and other properties, represented the difference between the aggregate necessities of this country for living expenses and development, and the aggregate value of its exported goods. It also resulted in such a development of productive capacity as to enable this nation to discharge the indebtedness within a few years of great activity during the world crisis. The estimated national wealth at the time these payments were made, was probably about five times the estimated national wealth at the times when the indebtedness was incurred.

The German budget can not be balanced and a surplus provided for reparations without taxing the German people heavily. What is taken from them in taxes is withdrawn from them in purchasing power and thereby the domestic market for German goods is restricted. To the extent that payments are made to the Allied Nations, the purchasing power of these nations is increased. Prices in Germany would ultimately fall and costs as well, and prices would tend to rise in other countries, under which circumstances Germany's exports would increase.

Everything seems to support both the justice and the mutual advantages of establishing equality of burden. That some risks must be taken at some point along the line of this effort is certain. An equality of the burden of taxation, whether it be paid for reparations or not, tends toward industrial equilibrium, and if being paid in taxes, it accumulates only as a credit and can not be paid in reparation, then no citizen of an Allied Nation can say that justice and morality have been violated in the forgiving of a debt, but will know that the debt fails of collection because of the real poverty of the debtor. The obligation should be stated upon a sound and moral basis, and the method of collection arranged so that relief may be had, at least temporarily, whenever payments would be destructive of the banking and currency system.

Under any circumstances the tax payment ought to be made and deposited to the credit of reparations, but only such an amount could actually be paid upon reparations as would be determined by the development of international commerce. The control of actual payments would be in the hands of those who were charged with maintaining the solvency of the bank and within reasonable limits, the parity of the currency. No one knows what these actual payments would be; it can not be exactly estimated. All that is known is that it will be within Germany's capacity and not more than in justice and equity she ought to pay. It will be determined by a practical demonstration and cease to be a subject of speculative controversy. For decades prior

to the war there was an increasing scale of expenditure by cities, states and the Reich and a growing volume of German investments abroad, and these things could not have existed unless the collection from taxes had been ample and the margin of exports, visible and invisible, a substantial amount over all imports. The members of the Committee seem to believe that with normal economic and business conditions restored, this ability to support its government and establish a favorable balance of trade would again be demonstrated by Germany. If it should not be, then there will be no trouble created by an internal surplus and no problem of converting an internal credit from surplus into a foreign payment, for there would be no surplus and no payment. But if Germany sustains herself as a strong, virile and productive nation capable of such vigorous industrial effort as she put forth before the war, then there will be such a surplus and the problem of making payments abroad will doubtless require careful study. It will be a recurring subject for discussion.

The relation between productivity and the power to pay taxes is quite as direct as that between the exportable surplus and the power to make payments in foreign exchange. It is the extent to which production is stimulated that determines both the maximum of revenue and the surplus of exports over imports, and if Germany assumes and carries an aggregate tax-burden, as large relatively as that borne by France to-day, there will be surplus of revenue above the necessary expenses of maintain-

ing the government. This surplus will be placed to the credit of the reparation account. It will be deposited in the new bank and one of the important functions of the bank, according to the plan as now outlined, will be to arrange for the payments out of this fund to the foreign creditors of Germany in such a manner as to protect the solvency of the bank and maintain the parity of the German currency, not out of a tender feeling toward Germany but because only in this way can German production be sustained and only by increasing production can Germany make substantial payments.

There are so many mutual interests that some agreement for common effort must be made. There will be felt a little later an influence which may to some extent lighten this burden of converting an interior credit into an exterior payment. This is, that when the payments become large it will be realized that the receiving of them will mean that foreign goods are to some extent displacing domestic goods in the home market. Just as France found it impracticable to have Germans come into France to rebuild its devastated area, because the French laborers needed this employment themselves, so at some later time there may be a demand that payments in goods should not be made too rapidly for fear of dislocating the industrial organizations in the nations that are receiving the payments.

This, of course, is a most important matter for all the creditors of Germany and for the United States as well, for it is the creditor of Germany's creditors. This aspect of the problem is well expressed in to-

day's issue of the *London Times,* first by Mr. F. C. Goodenough's statement at the annual meeting of the stockholders of Barclay's Bank, and second by Mr. Walter Leaf in his annual report to the stockholders of the Westminster Bank. Mr. Goodenough said: "Besides the payment for imported foodstuffs, raw materials and manufactured articles, which were normal before the war, we have now to provide also for the interest on our debt to America. . . . The total annual provision that will be required for the next ten years to meet the debt will amount at current rates of exchange, to the sum of approximately thirty-seven million pounds per annum. . . . The real burden of the debt, however, is measured by the volume of goods or services needed to discharge it, and the amount of the burden will, therefore, fluctuate with variations in dollar prices, as the debt is payable in dollars." Mr. Walter Leaf remarks: "One thing is certain; that reparations paid by Germany can come through one channel alone—through an excess of German exports over imports. It is only by taking German goods that we can receive German payments. . . . It happens that we have before us at this moment an excellent illustration of the way in which international payments are made in goods. It will be within the memory of all of you that some two years ago the United States passed what is known as the Fordney Tariff, a very high tariff designed with the special intent of excluding foreign goods, and in the belief that other countries could not dispense with the products of the United States. Now how has the Ford-

ney Tariff worked? I have before me the figures of trade between the United States and Great Britain for the first nine months of 1923, and I compare them with the first nine months of 1922. You will suppose, or at least the authors of the tariff certainly supposed, that there will be a great falling off in the exports from Great Britain to the United States, while the exports from the United States to Great Britain will be maintained. Well, what are the facts? The exports from the United States to Great Britain have in that period fallen off by more than sixteen million pounds, while exports from Great Britain to the United States have increased by over ten million pounds. The balance of trade in those nine months has moved nearly twenty-seven million pounds in favor of this country. Surely this must give Mr. Fordney serious matter for consideration. Naturally this can not be the actual result of the tariff; it proves that there are opposite influences which overcome the obstacles put in the way of imports from abroad. There can be little doubt that this influence is to be found in the remittances which Great Britain is making to the United States for the payment of the debt. So long as the United States requires payments from us, so long must they take it in the form of goods. And in the meantime the Fordney Tariff has naturally increased prices and put up the cost of production in the United States, and has thereby hindered their power of competition with us in neutral markets. So that the tariff has been by no means an unmixed misfortune to British trade, and it offers an impres-

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Chairman First Committee of Experts

sive example of the futility of political measures which try to counteract the irresistible tendencies of economic law."

Both of these eminent financiers declare that debt between nations can be paid only in goods; one states that annual payments by Great Britain to the United States will amount to about thirty-seven million pounds; the other reports that during the first year when these payments became effective there was a movement in the balance of trade between these nations in favor of Great Britain, amounting to twenty-seven million pounds in nine months, or at the rate of thirty-six million pounds a year, and this in spite of tariff obstructions.

One of the merits of the plan under consideration of the Committee is that it brings under the control of a responsible organization the time of making payments and the amount of payments to be made at a particular time with due regard to interests of both debtor and creditor. It may be the debtor can not afford to pay nor the creditor to receive. Time will disclose this. But it would seem dangerous to fix now, definite sums which must be paid at definite periods, no matter how destructive the consequences might be to the nation that pays, and to the nation that receives. The creation of an internal credit in Germany need not be drawn on if the payment would injure the creditor; other forms of payment could be devised or the credit could for the time being be left unused. It is not to be doubted that if only certain large initial payments could be made to put in order

financial budgets in some of the Allied Nations, this credit would be left in Germany until a favorable time and method could be found for the withdrawal. Perhaps when the inescapable burdens of receiving are as generally recognized as are the difficulties of making payments, nations will be more inclined to abate their claims. If the inference to be drawn from the discussions of the English bankers from whom I have quoted is sound, the United States would as a consequence of complete debt collection, experience an unfavorable movement in the balance of trade of nearly half a billion dollars a year for a period of about sixty years. Whether she would continue to desire such an amount of foreign goods to displace her own, it remains for the future to determine. There seems to be no disposition now to recognize this difficulty either on the part of the United States or other creditor nations against which the same forces would operate.

But at the same time the alleged danger of debt collection may be greatly exaggerated. It seems paradoxical to assert that an influx of wealth into a country would produce poverty. It is doubtless true that much of the goods by means of which payments are made would not compete with goods of domestic manufacture and the use of such imported goods would add to the comfort and improve the living conditions of the people. The sale of European securities would tend to prolong the period during which the payments could be made out of exportable surplus.

At the present moment there is need for large

credits to be transferred to France and means may be found, and ought to be found, to accomplish this. No proposal ought to be made or can really be considered that does not include provisions for the safety and security of France as the largest creditor of Germany. In the first place, public opinion in other countries would condemn it as unjust and in the second place France would veto it. She has expended huge sums for the rebuilding of the devastated areas and for the payment of pensions. These expenditures she has charged to Reparation Account and in this way she balances her budget. There is a great sentiment of sympathy for the afflicted people of these districts, and feeling of the obligation resting upon those who escaped such burdens, to restore the homes and property of those who suffered such losses. This sentiment was too strong to be guided by prudence. They have built too fast, from a banker's point of view, but no threat of disaster could have stayed the hand of France once it took up this work of repatriation of the people of the devastated areas.

Up to December 31, 1923, the aggregate amount charged by France to the reconstruction account, to be collected from the reparation credit, is one hundred eighteen billion francs; sixty-six billion of this was for reconstruction proper, thirty-five billion for pensions and seventeen billion for accrued interest. The twenty-six billion gold marks belonging to France of A and B Reparation bonds, at even four and one-half francs to the gold mark just equal this sum. And in the tentative budget for 1924,

which has been furnished from official sources, there is provision for an expenditure of eight billion francs more during this year. These are the expenditures which under the Treaty of Versailles were to be the first charge against Germany by way of reparation, and there can be little doubt that the pitiful necessity for reconstruction, as distinguished even from pensions, was generally regarded as creating the moral basis for holding Germany responsible for the damages inflicted. To what extent these damages were actual and the proceeds of reparations required to repair them, is therefore a matter of general interest, especially since so many seem to regard the fixing of reparation obligations as merely a punitive measure. But the repair of these devastated towns was an obligation imposed upon and accepted by Germany, and the amounts required to meet this particular charge will certainly exceed the total that France is demanding from Germany.

The greater part of this work was done at a time when the general average of the exchange value of the mark was eight cents or one-third of a gold mark. The expenditure, therefore, was equal to twenty-two billion gold marks for construction, eleven and two-thirds billion gold marks for pensions, and five and two-thirds billion gold marks for interest, making thirty-nine and one-third billion gold marks in all. These are the expenditures up to December 31, 1923. The estimate from official sources is that the work of construction is about 62% completed—as of January 1, 1924. The total

cost of reconstruction alone completed and without considering interest or pensions, could not, therefore, be less than the equivalent of thirty-five billion gold marks, while the total amount of expenditures for reconstruction, interest and pensions would exceed fifty billion gold marks. Monsieur Poincaré's proposal was that France would accept twenty-six billion gold marks and such additional amounts only as might be required of her to settle inter-allied indebtedness. A tour through these sadly shattered towns and villages impresses one with the burden of suffering as well as of paying that France has been carrying, for even now, six years after destruction, these towns are only a little more than half rebuilt, and the greatest inconveniences have been endured by their citizens.

The other items of this tentative budget only emphasize the weight of the burden France is carrying. The budget shows that France's income from direct taxes is fifty-one hundred million francs, from indirect taxes seventeen thousand, one hundred twenty-nine million francs and from miscellaneous taxes thirteen hundred seventy million francs which may be augmented by legislation now being discussed providing for a 20% increase. Her administration expenses, on the other hand, are ten thousand eight hundred thirty-one million francs and interest on internal loans thirteen thousand five hundred fifteen million francs. In addition to this there is accruing interest upon her foreign loans expressed in dollars and pounds and the reconstruction expenses just referred to.

To-day Mr. Young spoke about the work of the Committee in investigating the railroads and how this property might be used in reparations. This is a subject which, of course, must be taken up again in detail but for the present it would be enough to epitomize the preliminary report of engineers to the general effect that there existed in Germany about thirty-eight thousand miles of road, of a value (on the 1913 basis of costs) of about five billion dollars and with an earning capacity, assuming restoration of productivity, of about two hundred and fifty million dollars, of which fifty million dollars ought to be retained for construction and readjustment of the system. Owing to the processes of inflation, this property is free from any indebtedness. It was purchased by the Reich in 1921 at a cost of three hundred fifty-eight billion (our trillion) marks, now worth less than one hundred dollars, but more than sufficient at that time to discharge all the indebtedness of the states incurred in acquiring the system.

How could this resource be used? Could bonds be issued up to about three billion dollars and both bonds and stock pledged with the bank as security for reparation payments? Could such bonds be sold in the United States or England or France? For what period ought such bonds be issued and at what rate of interest and amortization? Could this asset be used to meet the more pressing needs of Germany's creditors?

A continuing delivery of payments, whether in cash or goods, is as essential for the welfare of Germany's creditors as it is necessary for Germany to

obtain a temporary relief from excessive payments. In some form it appears to be necessary to provide for current payments to creditors by pledging property, which insures future payments, and securing cash by the sale of such pledges. Whether this be by the pledge of railroad earnings or of specified monopolies or of both, or by a general obligation of the German Government with such securities, is a matter yet to be decided.

The minimum of interference with Germany's control of her own affairs is probably the policy that will bring the maximum of payments to her creditors, and in measuring thus carefully by actual test the capacity of Germany to pay as indicated by her increasing prosperity, there must of course be established a system whereby all payments made on reparation accounts or on account of any of the established claims against her as fixed by the Treaty or events that have followed, should be treated as a whole. She could not be held responsible for an annual payment estimated to be at the maximum of her ability to pay and then be forced to pay additional sums either for the expenses of armies of occupation or for deliveries of materials. All the demands ought to be reduced to a cash basis and the aggregate of all to be within her capacity to pay. Unless this condition be recognized, Germany could not be fully restored in the confidence of the world and her industrial organizations could not reestablish their credit. But if this limitation be recognized, the public and private credit of Germany would be restored and very quickly after the new bank is functioning.

With credit restored, bonds issued upon the railroad system or upon the income of monopolies in Germany, could be sold and the proceeds used by the creditors of Germany in such a manner as to reassure the world that all the nations of Europe would be at last on the road to recovery. The interests of France require that Germany should be restored, not only in order that reparation may be collected, but that normal economic and business relations may be resumed, and in the same manner, the prosperity of France is necessary for the welfare of Germany. Not much would be gained for the welfare of Europe if a plan were carried out which restored Germany temporarily to normal economic functioning and permitted France to fall into economic confusion.

Before the opening of this conference, there seemed to be great difficulties in the way of reaching a common agreement. The divergent views of the different governments as to the plan of fixing and collecting reparations seemed irreconcilable. England's insistence on, and France's rejection of, the process proposed for measuring again, and this time definitely and finally, Germany's ultimate capacity to pay, and limiting the efforts to make collections to such a sum when ascertained, had produced stubborn advocates and opponents, and created irritation and apprehension. At the present moment there is much hope that the Committee of Experts may reach speedily a unanimous agreement upon a plan which can be developed and explained without involving the feeling of resistance that has

been evoked by the discussion of the necessity of fixing ultimate capacity to pay as the first step toward settlement. For the Committee has already agreed that fixing an amount of annual payments, to be determined by an attempt to establish in Germany a scale of taxation commensurate with that borne by the Allied Nations, is the logical approach; they have also agreed that the stabilization of the currency must be accomplished as the first step toward the restoration of normal conditions and that the organization of a new bank of issue is necessary to accomplish this; and that such a bank being established, both Germany and her creditors could be protected against the collapse of Germany by reason of demands being made upon her beyond her capacity to make payments. Such a bank, being under the control of an international Board of Directors, could suspend the payment of reparations whenever such payments would destroy the stability of the currency, endanger the solvency of the bank or disrupt the industrial organization of the nation. And the real measure of Germany's capacity to pay could thus be made by actual experience, and the contentious and theoretical discussion of it removed from international conferences. Having apparently come to an agreement upon these important preliminary and fundamental principles, the Committee is now considering the resources of Germany that can be used to meet the immediate needs of her creditors and the details of the practical methods to be adopted whereby the general plan can be put into effective operation.

CHAPTER III

TRIP TO BERLIN—THE CONFUSION OF INFLATION—CHANGED RELATIONS OF PEOPLE TO GOVERNMENT—RECEPTION BY CHANCELLOR MARX—POINCARÉ'S COMMENTS ON COMMITTEE'S WORK—HOPEFUL ATTITUDE OF BOTH FRENCH AND GERMAN GOVERNMENTS—RUHR INVASION—PASSIVE RESISTANCE AND CONSEQUENCES—INFLATION—CURRENCIES IN CIRCULATION—THE TEMPORARY STABILIZATION—ENSUING CRISIS—SLOW RECOVERY—RENTENBANK—TAXATION SYSTEM—NEW SCHEDULES—COMPARED TO FRENCH—RESULTS IN AUSTRIA.

Berlin, January 31, 1924.

The Committee with all of its followers left Paris Monday evening and reached Berlin Tuesday evening about ten o'clock, and most of the members went to the Esplanade Hotel. A full company of uniformed police and an army of correspondents and photographers met the train. There seems to be a keen interest here in the activity of this Committee. The country between Cologne and Berlin, and Berlin itself, has the general appearance of inactivity; few of the factories are in operation. The people really have a subdued appearance—several of our party have commented upon this. But the factories and buildings of all sorts appear intact and very much up to date. We met on the train a

German professor who said that the nearer we came to the study of German economics the more complicated it would appear on account of the effects of inflation. This was truly discouraging, for we had read many discussions of the German budget and of the German railways, for instance, which were not as a matter of fact discussions of these things themselves, but of the phenomena of inflation as affecting them. Any study of German statistics, the professor warned us, would be made most difficult by the uncertainty of results secured by attempting to translate movements measured by paper marks into gold marks of pre-war value. He doubted if statistics of the last year meant anything at all. He spoke of the efforts he himself had made to develop a formula for translating what was taking place into some plain statement that would give a definite meaning but said he had given it up. Taxes levied to meet expenses when the paper mark was at say twenty thousand to the gold mark, were collected when the gold mark was worth one million paper marks. Goods for export might be sold under similar conditions and statistics as to foreign trade were unreliable. When accounts run into eighteen figures the mere labor of compiling them adds so much to the burden of accountants as to cause great delay and many mistakes. It is a small matter perhaps but one that lays a heavy aggregate burden on accountants. It is simple enough, one may say, to record that $16.75 is now worth 70,350,000,000,000 paper marks, but how many dollars could be bought with 726,350,649,426,000 paper marks, etc.? The banks

are all behind with their public statements, delayed by this factor, or factoring.

Among other things, the professor said that the reorganization of the German Government was made necessary by the emergency under which the Reich was obliged to lay its hands upon taxable resources formerly reserved for the states. Speaking very generally the land tax and other direct taxes were levied by the states and the Reich collected only indirect taxes. Under the new constitution the Reich was given control over many forms of taxation formerly collected by the states. It was not a very carefully designed system but an adjustment hastily made to meet a sudden emergency, not deliberately adopted in recognition of the growth of public feeling and opinion. It was not an evolutionary process and it would probably be found later on to be much against both the habits and sentiments of the people. In some cases the loyalty of the people of Germany is to the states rather than the Reich, and the new adjustment has not altered this fundamental feeling.

Since we have been in Berlin our attention has also been called again to the political divisions in the Reichstag. In our own country both of the great parties contain many representatives of farmers, of laborers, of industrialists and in fact men of every social grade and business activity and even of varying political sentiments. In Germany it is quite different. The farmers have their party, the industrialists another, the extreme radicals are allied, and also the more moderate. This is not an attempt to

EN ROUTE STEAMSHIP *AMERICA*

Left to Right: Colonel Goldsmith, Rufus C. Dawes, Mr. Tileston, Mr. Young, General Dawes, Captain Rind, *S.S. America,* Mr. Crocker.

Meeting Place of Committee in Berlin

diagnose the political situation more than to say that the verdict of a majority in our country is accepted as the opinion which must prevail, because it is held by a majority of the people, all of whom must bear the burden of the decision. Whereas, in Germany, it may sometimes be regarded as a decision imposed upon a minority by the majority, which has a contrary interest, and does not share the hardship incurred by it. These two conditions make it very difficult for Germany to express itself and work out its salvation with the same unity of spirit as it displayed under the stimulus of war and the direction of an imperial government, and raises the question as to whether it would not be better for Germany to act or appear to act, in carrying out some of these necessary adjustments, under outside pressure.

February 1, 1924.

To-day a newspaper correspondent said he had just been talking with the ex-Dictator, Stresemann, and that Stresemann had criticized Doctor Schacht for going to Paris with his plan. For the first time, he said, Schacht had secured assurances of help from English and Holland banks, and had worked out a sensible plan, which he was about to carry into execution. Having revealed this to the Committee, he might now have to see it presented as the Committee's plan, which from Stresemann's point of view, vitiated it, because it would mean foreign control or interference with the German bank. But, the reporter stated, even this seemed tolerable provid-

ing only the Ruhr should be evacuated, commercial obstructions removed and government revenues restored. He said he did not know exactly to what extent the German demands would go, but that their feeling about the Ruhr was one of desperate determination and that all Germans were united on this point. For some days General Dawes has been saying the test of this Committee's work would come in the settlement they could propose as to the Ruhr, and he had good hope that the Committee may find a basis of settlement, but probably not one that would involve the complete withdrawal of all troops.

In the meantime, members of the Committee have ascertained that Doctor Schacht is in good standing with the government and is the logical person with whom the Committee ought to work in making plans for the bank.

On Tuesday they were invited in a body to call upon the Chancellor, Herr Marx, and were received by him surrounded by his staff in the very room wherein the great Bismark formerly ruled.

"Gentlemen," said the Chancellor, "I am glad that an opportunity is offered me of welcoming you here in the name of the German Government after a decision taken by the Reparation Commission on November thirtieth last has entrusted you with the task to look for ways and means of establishing equilibrium in the German budget, as well as for the measures to be taken with a view to stabilizing German currency. The German Government thankfully appreciates it that you have come here in order to examine on the spot the situation existing

in Germany. Our Government Departments will leave nothing undone that may be of assistance to you in the accomplishment of your task, which is so difficult and which involves so heavy a responsibility. Your desiderata will be considered and your questions will be answered with the utmost promptitude and in a spirit of unreserved frankness. In order to support you in your work the German Government has caused materials and data for a study of German economy, German currency and German finance to be collected, which collection of data will shortly be handed to you. With a view to facilitating the official relations between the Committee and the German Government Department, the German Kriegslasten Commission (War Burdens Commission), whose Chairman is the State Secretary, Mr. Fischer, has been charged to represent, vis-a-vis you, the German Government. Moreover a special representative in the building is placed at your disposal for the performance of your work, in order to be the recipient of your desiderata."

The Chairman of the Committee, General Dawes, replied as follows:

"Your Excellency, the Committee desires me to express our appreciation of the opportunity to meet you and your associates in the German Government. As members of this Committee, we feel the great importance of a common understanding among the Allies upon some solution of the problems before us, in which understanding it is most desirable and important that the German Government participate. It is our hope that such an understanding will be

attained. We thank you for the assurances of your aid and cooperation."

These expressions on the part of the Chairman were sufficiently reserved to escape criticism of his fellow members, but Herr Marx was not so fortunate. The papers or, at least, some of them, found fault with him for having received the Committee. The material prepared by the government to which he referred was a full and well prepared book giving essential facts concerning the commerce, currency, finances and industry of Germany. A large building, formerly used by the Ministry of Finance, has been put at the disposal of the Committee and their assistants, about seventy people altogether.

In Berlin, as well as in Paris, there seems to be a disposition on the part of the government to facilitate the work of the Committee.

On January eighteenth, Monsieur Poincaré made an address before the Chamber of Deputies, from which the following extracts will be found to be interesting:

"I do not doubt that the inquiry undertaken under auspicious circumstances by the Commission of Reparations will greatly facilitate our task of adjusting arrangements with Germany. . . . But it must not be forgotten that the initiative in this matter belongs to the French Government. It was this government which, on the tenth of November last, asked in conformity with Article 234 of the Treaty of Versailles that the Reparation Commission should designate experts, not as has been sought before, to evaluate the capacity of Germany

to make payments, but to make an estimate at the present time of its actual resources. I did not wish to accept beforehand the German idea taken up a year ago by the British Government of a conference which should have as its object the definite valuation of the pretended capacity to-day of Germany to make payments; under that cover, one could not but arrive at results exactly contrary to economic science. . . . The excellent speech of Mr. Dawes, one of the American experts, moreover, permits us to think that now all discussion of this sort is eliminated, that Article 234 of the Treaty will be respected and that the sophism about the definite ability to pay will not deceive in any degree the two Committees of Experts, and that they will be able to continue in entire independence a work, in itself, very vast and important. We are greatly pleased to see this cooperation of the Allies establishing itself within the limits of the Treaty and with the very valuable presence of our friends from America. . . . In our opinion the work of these Committees will be in any case a first step toward a general settlement. . . . Some newspapers have reproached France for not having presented a constructive plan. Long months ago we put one before our Allies. We demanded a minimum of twenty-six milliard gold marks corresponding to our percentages in the A and B obligations. We agreed not to have recourse against Germany for the rest of our credit, except in such measure as we ourselves should be required to pay inter-allied debts. The work of the experts, therefore, should turn on the

following points: to seek to introduce into Germany a sane and stable money, to establish a control of the German budget during a certain period, to establish likewise a control over certain German resources in such manner as to make of them financial guarantees, either through the payment of annuities or preferably, by the emission of loans. Such resources which can be used as guarantees are among others, as the Belgian-French studies indicate, the customs duties, the railroads, coal, the electric industry, the tobacco monopoly and other receipts of the same sort. . . .

"We shall demand, so far as we are concerned, from the experts to have the system of control put in force by the French and Belgian Governments, over those guarantees which we hold in the occupied territories made a part of their system. The French and Belgian authorities, or preferably, if the other Allies will consent—and we hope that they will consent—the inter-allied authorities shall keep in hand this control, it being understood that the necessary expenses of the occupation and exploitation of the guarantees being paid, the excess shall be turned over, as I have always said to the Reparation Commission, and divided among the Allies, all the Allies, in proportion to their rights. Once in possession of the work of the experts, the Commission can estimate with full liberty the amount of the payments in capital, which it shall consider it possible to demand immediately from Germany. These amounts of capital, we believe, might properly bear upon the railroads of the occupied territories, which ought to

be given over to an inter-allied company, and which would thus serve at the same time as payment for reparations, and as a guarantee for the security of France and Belgium. These amounts ought also to rest upon shareholdings in certain mines of the Ruhr in such manner that France may be assured in the future of receiving coal which its industries need. They ought to rest upon other shareholdings given to the Allies, either in certain industries or in certain products of Germany. . . . We shall ask that the task of the experts and of the Commission, so important as it is, shall be accomplished as rapidly as possible, without any reconsideration, I repeat it, of the question of fixing the total German debt, and without taking up discussion of the theoretic problem of which Mr. Dawes spoke so wittily."

These remarks he made at the close of a very long address, of which we have received only an imperfect translation, the earlier part of which was devoted to a defense of the French policy of invasion. He stated that the possibility of invasion had been under long discussion between the Allied Governments as the proper measure of enforcing deliveries under the Treaty, and having been in this manner threatened against Germany, independent action was taken by Belgium and France only when it became apparent that Great Britain would not cooperate; that it was essential that the inter-allied front be reestablished and that the work of the Committee of Experts would be helpful in bringing this about. He stated that actual deliveries of goods and materials amounted to only twenty-eight million

gold marks or ninety million francs in 1922. During 1923 the French have taken in payments in kind not less than one hundred thirty-five million four hundred thirty thousand francs. He discussed passive resistance briefly, declaring it was a suicidal policy which France deplored, and dismissed as fables the charges that France was promoting a movement for independence in the Palatinate, denying that France had any desire to annex the territories in question or to have them brought under her political control.

This speech was not strictly a defense of the French policy in general, but a reply to an attack against the policy by Monsieur Herriot. It did not cover all points under international discussion. It seemed important coming at just this time because it discloses a conception of the problem and methods for solving it quite in harmony with the general course being pursued by the Committee, and seems to suggest the possibility of relaxing the stranglehold upon the Ruhr, while at the same time emphasizing the limits imposed for the Committee's work.

Already we learn upon the best of authority that the French are showing a desire to conciliate feeling in the Ruhr. Export taxes are cut to a minimum. Administration has been made more informal and easy. The withdrawal of troops continues. There is now only 40% of the number there was two months ago. Reports from the newspapers and from the Consul at Coblenz indicate an increasing willingness on the part of France to modify the severe régime established for the purpose of overcoming

the passive resistance which was recently suspended.

This expressed preference of France for the substitution of an inter-allied for the French and Belgian control of the guaranties seized, indicates a strong desire on her part for the restoration of allied harmony and unity of action, and her more moderate attitude in the Ruhr to-day confirms this impression. She would sacrifice a great deal to bring this about. It was not until after the cessation of passive resistance to the invasion of the Ruhr that France secured important results from its decision taken in January, 1923, to take possession of this territory. During the ten months from January to November she suffered from the continued criticism of the English Government, and the passive resistance of the German Government deprived her of immediate returns, and threatened her with grave disasters, the most dreaded of which was the widening of the breach between herself and her allies. But whether her policy was right or not, her people have steadily supported the government in carrying it out, and at the present time undoubtedly feel that events have vindicated it, and that the invasion has compelled an attitude of acquiescence on the part of the German Government and people in the terms of the Treaty of Versailles and forced the German Government to act according to the Treaty rather than public sentiment. With this result there is every appearance that the present French Government is satisfied. It was with this object in view that the policy of invasion was announced. But it

is hardly to be supposed that her people would allow or her allies demand the entire withdrawal of all troops from this section. It seems to be very generally recognized that this course of action, so expensive to France, has created in Germany the impression that its government must act under pressure of outside force and that the German will can not prevail, and that both to satisfy public opinion within France, and in order not to deceive the people of Germany, some outward show of force within that territory must be maintained. Germany's attitude is more compliant now than it was in 1921 and 1922, and no economic settlement is possible unless it remains so.

The invasion of the Ruhr was the culmination of a series of disputes between Germany and the Allied Powers, and the beginning of a new relationship between the Allies themselves, as well as between Germany and the Allies. The tension of this great dispute is relaxed, now that passive resistance has been terminated, and in consequence the economic pressure is lightened, but some review of these events seems necessary to throw light on the present status of the controversy.

After many previous disputes as to payment of reparations and deliveries of coal, according to the schedule of agreements, the Reparation Commission on March 15, 1921, declaring that Germany's claims as to the amounts previously paid were grossly inflated, demanded the payments of one billion gold marks by March twenty-third, and twelve billion gold marks by May first. And on March 24,

1921, Germany, having failed to make the first payment, was declared to be in "default in respect to the performance of her obligations and agreement." Under the terms of the Reparation Recovery Act, Great Britain at this time imposed a tax of 50% on imports from Germany to be credited to Reparation Account, and on April sixteenth the Reparation Commission ordered the gold reserve of the Reichsbank to be placed in Cologne and Coblenz as security. On May 3, 1921, the Reparation Commission notified the Allies that Germany was in default in respect of her obligations to the extent of at least twelve billion gold marks, and on May 5, 1921, an ultimatum was issued to Germany threatening the occupation of the Ruhr in case of non-compliance. On May eleventh the German Government accepted this decision of the Reparation Commission, and England withdrew its 50% punitive import levy against German goods. During the balance of the year 1921, there were agreements made for the delivery of coal and other goods and adjustments for the extension of time within which specified payments were to be made. And on March 21, 1922, the Reparation Commission, announcing the details of a part moratorium or cessation of payments, provided that in case of default of deliveries in kind brought about by obstruction on the part of the German Government, additional equivalent cash payments would be exacted at the end of the year.

In August, France refused to grant further moratorium without guaranties. Great Britain proposed to reduce the total cash payments to not more than

26% of exports, which was not acceptable to France, but a six-months release from cash payments was granted to Germany. On December 26, 1922, the Reparation Commission declared Germany to be in voluntary default in timber deliveries to France in 1922, in consequence of which Great Britain suggested that the threat of March 21, 1922, should be executed and additional cash payments required. But France and Belgium demanded that the threat of May 5, 1921, should be enforced and the Ruhr invaded. In this critical time, January second to seventh, a meeting of the Premiers was called, and proposals for a modified settlement made by Great Britain and by France and by Italy, but no agreement could be reached. On January ninth, the Reparation Commission declared Germany in default on coal deliveries, Great Britain voting in the negative, and on January eleventh French and Belgian troops entered the Ruhr.

As to whether this action was justified legally under the Treaty is a matter of dispute and probably will always be controverted. France claimed that Part VIII of the Treaty gave her the right to act in this manner under the circumstances, but by paragraph 12, annex II, the Reparation Commission is constituted as the tribunal to interpret the provisions of Part VIII and by paragraph 13 it is provided that on questions of interpretation *a unanimous vote of the Delegates is necessary.* So, therefore, so long as France and England differ, there can be no unanimous vote, and consequently no authoritative decision. Germany has always main-

tained that the Ruhr occupation was illegal, and English jurists have made arguments to the same conclusion.

Paragraph 18, annex II, Part VIII, of the Treaty reads:

"The measures which the Allied and Associated Powers shall have the right to take, in case of voluntary default by Germany, and which Germany agrees not to regard as acts of war, may include economic and financial prohibitions and reprisals and in general such other measures as the respective governments may determine to be necessary in the circumstances."

Germany, having been formally declared by the authorized agency under the Treaty to be in voluntary default, France and Belgium with the acquiescence of Italy determined that the measure necessary in the circumstances was the occupation of the Ruhr. They claim that under international law, outside of the Treaty, there is always the right to take aggressive action in case of the voluntary default or failure on the part of one signatory party to carry out an agreement, and therefore there could not be any implied qualifications to words so clear in themselves as "such other measures as the respective governments may determine to be necessary in the circumstances" and moreover they say that by Article 248 of the Treaty, a first charge on all the German assets is created in favor of reparations and that this amounts to a mortgage which implies the right, in case of voluntary default, to seize the physical assets of the debtor.

The British argument is, that the boundaries of Germany are definitely fixed by the Treaty and a provision made that certain parts of it should be occupied for a period of fifteen years as a guaranty for the carrying out of the Treaty, and that Article 430 in Part XIV reads: "In case during the occupation the Reparation Commission finds that Germany refuses to observe the whole or part of her obligations under the present Treaty with regard to reparations, the whole or part of the areas specified above will be reoccupied immediately"; that the areas specified do not include the Ruhr and therefore the Ruhr is outside of the maximum military occupation authorized for a reparation default; that Part XIV relative to military guaranties is a specific provision on a special subject and prevents the application to that subject of general words found in other parts of the same instrument; that there would be no point to the language of Article 430 permitting occupation if that were already provided for by paragraph 18, Part VIII of annex II; and that paragraph 18 is properly interpreted "may include economic and financial prohibitions and reprisals and in general such other like measures," since where general words follow specified words, the general words are limited by the genus described by the specific words; and further that it is unthinkable that in a treaty framed to preserve the peace and territorial integrity of Europe, there should be an express provision permitting any and all of the Allies entitled to reparation to seize any part of the German's territory at will. They add

that in the case of ambiguity or doubt in treaty interpretation the doubt should always be resolved in favor of the party upon whom the terms are imposed, and that the obligation of Germany was not to France and Belgium and Italy, but to the joint partnership of all the Allied Powers, and one partner may not forcibly collect the partnership debt for his own account. And in reply to the point that on May 5, 1921, England had voted, with the other nations on the Reparation Commission, in favor of threatening the occupation of the Ruhr on the occasion of a default, their argument is that England had joined in this threat not on account of a *reparation* default, but because of a general failure of Germany to carry out the Treaty, by the destruction of war materials, by the manner of conducting the trials of war criminals, etc. etc., on account of which Great Britain was proposing to denounce the Treaty and act outside of it. In the case of reparation default, it was claimed, the Treaty contains its own sanctions, namely, economic and financial reprisals and the reoccupation of specified territories.

There was no dispute between the Allies about the fact of default and the general failure of Germany at that time to carry out in good faith the terms of its agreements under the Treaty, but an irreconcilable controversy as to the legal methods of dealing with such failure and default. The mere reoccupation of limited areas west of the Rhine appeared to the French to be a totally inadequate remedy, and particularly in view of the fact that the occupation of the Ruhr had been threatened as an act of re-

prisal; accordingly France and Belgium, with the announced purpose of compelling the German Government to accept the terms of the Treaty, substituted decisive action for the long series of futile conferences, which culminated in the failure of the governments to reach any agreement in the conference of January second to seventh. At this conference the French were willing to accept their proportion of the A and B bonds and to surrender all claim to C bonds in consideration of the cancellation of inter-allied indebtedness, but insisted upon guaranties involving some control over German finance, territory and industry, to which the British could not agree. The British proposed indemnity expressed in a new series of bonds with four years moratorium and in an amount of about fifty billion gold marks. But the Germans gave no evidence of being willing to accept even the British minimum. To the French they appeared to be trying to evade responsibility under the Treaty and to escape the financial burden of restoring northern France. This expense they felt the Germans were better able to carry than they were themselves. By taking the Ruhr, a vital part of Germany's economic structure, they expected, not to collect reparations directly but to create in Germany the willingness to pay. They believed that Germany's default was due to the influence of the great industrialists, at that time very prosperous and powerful, and that the occupation of the Ruhr would force the industrialists to support the government in a policy of paying reparations.

Doctor Marx
Reichs Chancellor

There was at that time every appearance of a break in the Allied front, a failure to agree on the amount of reparations or the sanctions to enforce payments, a dispute as to the legality of invasion and the beginning of the discussion as to "capacity to pay." And Germany was quick to act upon the theory that this breach could be widened. Protesting to the world that this invasion was illegal, its government established the policy of passive resistance. The railroad employees were ordered to discontinue working. Even sabotage appears to have been encouraged by industrial leaders and by the government. Striking workmen were paid unemployment doles which were called "indemnities for fidelity to the Reich."

This passive resistance was an economic warfare in which the Germans were as much deceived in their estimates of opposing forces as their generals were in 1914. It was intended by disturbing business in England and America to isolate France and create disagreement and dissensions among the Allied Nations. But the repressive economic measures put into effect by France as an offset to the strikes and sabotage, forced Germany to the expenditure of huge sums which in the end were supplied by the printing presses. It was not the occupation of the Ruhr, but rather the resistance to it, that caused the mark to drop into the abyss. When on January 11, 1923, France invaded the Ruhr, the mark had already fallen in purchasing power to the point where it would require four thousand to equal one gold mark; by April it would have taken six thousand;

July, eighty-four thousand; August, one million one hundred thousand; September, twenty-three million; October, six billion; November, five hundred billion and in December one trillion. But although the contest was burdensome for France, she sustained it without great disaster, and the hoped-for intervention from England or America did not appear. Passive resistance was unconditionally abandoned in October. It was for Germany a costly failure and far more expensive than the payment of reparations or passive submission to invasion from the very outset could have been. Her currency system was totally broken down, her industries deprived of the necessary raw materials, there was a great increase in unemployment, the transportation system was rendered ineffective, the farmers refused to deliver food materials in exchange for the depreciated currency, and political collapse and social chaos were impending. It is doubtful if the contest could have been prolonged. There was at this time much real suffering in Germany, but it was of short duration, for the suspension of passive resistance, the stopping of the printing presses in the manufacture of paper marks, and the organization of the Rentenbank have brought about a very sudden and marvelous improvement which has lasted until this time, and if only some settlement can be made, may continue until normal conditions are fully restored.

The effects of this warfare both in France and Germany seem to prepare the way for some rational settlement. The German Government realizes the

necessity for some adjustment and that almost any settlement is to be preferred to the conditions of the past year, when her revenues were in part withdrawn from her, her transportation system dislocated, her people in the great industrial centers idle and subsisting on doles which could be supplied only by a process which was gradually expropriating the property of its middle classes and exhausting the working capital of the nation. And upon the other hand, the sentiment of France is more compliant for she feels that her will has prevailed and her policy been vindicated. The criticism which threatened to isolate her from the sympathy of the world has dwindled and France obviously desires to see the allied unity of action and harmony of motives restored. Her needs also are so great and pressing as to make her anxious to see such conditions restored in Germany as to make subsequent reparation payments possible. To accomplish this it is so obviously necessary to remove the economic barriers set up in the Ruhr during the period of invasion and passive resistance and to restore the revenue of all the German territory and business to the German Government, that there is little fear at this moment that France will insist upon economically restrictive conditions in the industrial areas of Germany. Both the expressions of her statesmen, her recent action in moderating the control of the Ruhr, and the guarded but constructive attitude of the French members of this Committee, afford good grounds for believing that France will make sacrifices to bring about a settlement which would

increase her chances of receiving payments, and bring her into better relations with her old Associates and Allies in the war. The experience of the Ruhr taught both countries to dread and fear the effects of a military settlement and to prefer to seek an economic adjustment.

To trace the causes and explain the process and effects of inflation will be the task of some philosophic historian at some later time and the tragical story will be full of lessons for the statesmen of the future. Whether it had, as most Germans believe, its origin in the deficit of exports as compared with imports, and if so the extent to which this deficit was caused by the accumulation of private credits abroad or whether it originated in the deficit of government revenues, and if so the extent to which defective financing during the war contributed to force it, or whether it was actually favored by influential industrialists because they saw a chance for profiting by it at the expense of their employees, are among the questions to be answered. The repetition of the same experiences in Russia, Austria and Germany provides the material for a study, which ought to be productive of useful lessons. Particularly now would it be interesting to know what the later effects of this inflation in Germany will be upon the industry and thrift and organizing power of its people.

The first effect of the distribution of an excessive amount of currency, aside from the payment of the expenses of government, was the increase of prices and the less rapid advance of wages, and this in-

creased the margin of profit to the manufacturer. At the same time the purchasing power of the mark for domestic goods within Germany did not decline as rapidly as its value declined when exchanged for foreign currencies. When the value of a mark was five cents for exchange with dollars, it may have had a purchasing power within Germany of as much as nine cents. Goods manufactured in Germany and sold abroad for foreign currencies produced a double profit, the usual one plus the exchange profit.

This resulted in great earnings for manufacturers, but ultimately in a loss to the nation, for the goods sold for pounds and dollars were produced by labor that was paid in marks of constantly depreciating value and sold at prices lower than the cost would have been had the labor been paid in the same currencies as that for which the goods were sold. And as these earnings accumulated, they were expended in enlargements of plant, and the necessity to express the value in some real property rather than to keep it in marks was so urgent that much of this construction is said to be unnecessary and wasteful. But it accounts in part for the fact that the railways and industrial plants of Germany are said to be in better physical condition than they have ever been before.

The first function of money to be destroyed was its usefulness as a medium for savings. Its steady fall soon convinced the public of the folly of saving it, and this fundamentally reversed the standard of conduct fixed by the wisdom of generations for the

building of fortunes. It encouraged waste and extravagance and stimulated speculation. So long as the disparity between the rise of prices and the advance of wages continued, the workers were employed, the factories in active operation and there was a deceptive appearance of great prosperity. But business was becoming more and more a speculation and wages were losing their purchasing power, so that as the demand for increased wages became more insistent, production fell off, and when the Ruhr was invaded and patriotic feeling was appealed to in order to put an end to production, financial and industrial chaos ensued. The financing of the induced unemployment required the issuance of currency in such amounts as to accelerate its already rapid decline in value and this declining value itself created the necessity for the issuing of more. If, at the end of August, one million paper marks equaled in value one gold mark, and by the end of September it took three million paper marks to equal one gold mark, then, of course, the actual purchasing power of all the money in circulation at the end of September would have been only one third of the value of the same volume of currency at the end of August, and there was an actual shortage of money. The currency in circulation before the war was about six billion gold marks. The total value as measured in gold marks of the legal tender paper marks in circulation on August 31, 1923, was two hundred eighty-two million gold marks, and in spite of the activity of the printing presses and the enormously increased vol-

ume of paper marks in circulation the total value of legal tender paper marks in circulation on October 31, 1923, was only forty-seven million gold marks. The more they printed the less its value, and the less its value the more they printed, until the final collapse in November when their money, having lost its value as a medium of saving, lost its value also as a medium of exchange.

The investigations of the Committee to report upon the exported capital of Germany has estimated that Germany profited, by the sale abroad of marks and credits in marks, to the extent of from seven billion five hundred million to eight billion five hundred million gold marks or about two billion dollars. This profit, in itself large, was no compensation to them for the loss and injury inflicted upon their own people, for it destroyed the savings that were invested in bonds or notes or credits at banks and the incomes from pensions or life insurance annuities, making paupers of most of the well-to-do middle classes. It may be said that this was a redistribution rather than the destruction of wealth, and that what the creditor lost, the debtor gained, and it is true that the aggregate of physical property in Germany was not impaired. No buildings or plants were destroyed by the process, and because of the instinct to invest capital possessed in monetary forms liable to depreciation, into fixed assets of permanent value, industrial organizations had actually improved and enlarged their plants and equipments. But the destruction of all such personal property as bank deposits, notes, bonds and

annuities of every kind, has utterly despoiled a very large portion of the German people of all their property and savings and at the same time has enriched others by freeing them from the payment of their debts. It has at the same time stimulated speculation in exchanges and in stocks to an extent that would have seemed inconceivable before this experience. Many have profited largely by these transactions. Those who have been freed from their debts while retaining their property, and especially those who have profited by speculation, have become suddenly very rich, an experience which nearly always produces a state of elational insanity, and now rush about spending lavishly and acting foolishly. Their conduct offends the Germans and creates in all Europe both resentment against all Germans and the mistaken conviction that great wealth must abound in any country which produces such spendthrifts in such numbers. The process by which wealth is transferred from the thrifty and industrious to such idlers and spendthrifts is a serious shock and perhaps a permanent injury to any country. It must corrupt business morals, shatter business organization and undermine the whole economic structure of the country. And while it is true that fixed capital remains unimpaired, working capital has been destroyed or withdrawn from circulation. The deposits in savings banks at the close of 1913 were nearly twenty billion marks and at the close of 1924, seven hundred sixty gold marks, and the gold mark value of the total deposits of eight large German banks at the present time are less

than one-seventh of the total deposits of the same banks in 1913.

The actual shortage of effective currency in the midst of the unprecedented volume of paper money, drove men to the importation of foreign currencies, but as these had a more permanent value, they were hoarded and came into only a limited circulation, and were the medium of speculation, rather than exchange. Many of the municipalities issued currency, then the great industrial companies and even private business organizations issued their own promises to pay. Some of these were secured and some were not, but such was the necessity for money that they circulated, for a short time at least, without much regard to the conditions of their ultimate redemption. The government also issued, and circulated as currency in small denominations, dollar treasury bonds in the aggregate amount of fifty million dollars, and treasury bonds of the states were issued for general circulation. The railways also issued money. But even assuming all these currencies were redeemable, they were exchanged upon a basis of value which made the total value of all the currencies less than one-half of the normal circulation of Germany before the war. All the printing presses in the world could not have turned out enough paper money to have restored the value of the circulating currencies to that of the money in use in 1913.

Perhaps the most surprising phenomena of the whole experience was the abrupt termination of the activity of the printing presses and the quick re-

covery of a certain degree of stability to the value of outstanding issues, and the improvement, in spite of the shock of price adjustments, of general business, which immediately followed.

The climax of the inflation appears to have been reached in October and at that time, we were told, the food situation in German cities was more acute than it had been at any time during or since the war, and chiefly for the reason that the farmers refused to exchange their products for paper marks. The unemployed men numbered about four million and business of every kind was almost suspended.

The termination of passive resistance in the Ruhr during this month relieved the government of heavy demands and the organization of the Rentenbank provided the basis for confidence, which has carried them through three critical months with steady improvement in all respects. This is the bank which Doctor Schacht described as not indeed a bank, but a piece of administrative machinery. It issues money upon the security of mortgages on real and personal property, the interest and principal of which are to be collected through the administration of taxes.

The Rentenbank was organized as a bank of issue by a "Decree on the Erection of the German Rentenbank" of October 15, 1923. It came into operation in the middle of November. It was organized to take over the debt of the government to the Reichsbank, to provide credit to the government, while it was balancing its budget and to furnish a stable currency. It was scarcely expected that it could accomplish finally all these objects; it was intended

more as a temporary measure. It is founded upon a forced mortgage placed upon all fixed and movable property in Germany. The value of this property by the last assessment available was eighty billion marks and the mortgage was made for 4% of this or three billion two hundred million gold marks. Each owner of property is to pay 6% interest upon 4% of the assessed value of his property, and receives an interest in the earnings of the bank, and the bank has no outstanding stock. Upon the security of this mortgage the bank was authorized to issue three billion two hundred million Rentenmarks. There was no gold available and no foreign exchange. These mortgages though by no means readily exchangeable were regarded as the best basis for currency available. Two billion four hundred million marks have been issued by the bank; eight hundred million are being withheld upon the pretext that mortgages on property in the Ruhr are of doubtful value and this amount of eight hundred million as compared to the full amount of the authorized issue is the relative value of Ruhr property to the total value of German property.

Of these Rentenmarks, one billion two hundred million was turned over to the government, three hundred million of which was without interest and discharged the government's debt to the Reichsbank, and nine hundred million was loaned to the government at 6% interest. The balance was to be loaned through the Reichsbank, one-half designated for the use of the agricultural and one-half for industrial interests. The Rentenbank is autonomous

but the director of it is appointed by the chancellor. Such was the actual shortage of money and so urgent was the need for it that these Rentenmarks were at once accepted. The farmers delivered the goods in exchange for them. The food crisis was passed. The needs of the government were for the time being met, and the Reichsbank was strengthened. The paper mark became stable at the ratio of a trillion to one. The government is much nearer to balancing its budget than it has been since the war, and the railroads are said to be earning their expenses. Practically the entire amount reserved for lending to industry and agriculture is unissued. It may be put out to meet the demands of the farmers next spring. At present they are trying to hold it back. The amount in circulation now is one billion three hundred seventy-four million marks.

The following table shows approximately the various currencies and the amounts of each in circulation at the end of January, 1924:

	Approximate value in millions of gold marks on the basis of: 1 gold mark=1 trillion paper marks.
Legal Tender	
1. Reichsbank notes (according to the return as of January 31, 1924)	483.7
2. Bank-notes issued by the four private banks of issue	.1
Other Currencies	
3. Notgeld issued against security in foreign currency:	
(a) Railways	68.
(b) Other Concerns	1.4
4. Notgeld unsecured:	
(a) In occupied territory	132.0
(b) In unoccupied territory	27.6

5.	Rentenmarks (according to the Rentenbank return as of January 31, 1924)	1,374.0	
6.	Dollar Treasury Bonds (*Dollarschatzanwiseungen*, Law of March 2, 1923)...	210.0	
7.	Gold Loan (*Wertbestandige Anleihe*, Law of August 14, 1923).....	318.0	
8.	Treasury Bonds and Interim Bonds issued by the States	50.0	
9.	Certificates of the Hamburg and Schleswig-Holstein Banks (*Verrechnungsscheine*)	35.0	
10.	Notgeld secured by 6% Treasury Bonds and to the extent of ten million of the gold loan:		
	(a) Railways	144.0	
	(b) Other Concerns	110.0	2,953.8
	Small Change in Rentenpfennigs.....		5.8
	Foreign Currencies held in Germany (Doctor Schacht's estimate)		1,000.00

These currencies circulate upon a parity one with the other and at a ratio of one trillion marks to the gold mark or four trillion, two hundred billion marks to the dollar. But all prices are named in marks and a "mark" means a trillion marks or one Rentenmark. The smallest denomination of paper marks in circulation is for ten billion marks and it is worth about one-fifth of one cent. This readjustment created another shock and crisis, and prices at the moment are high. Immediately after the organization of the Rentenbank, according to the reports of the German Government, the real wages measured in gold marks for all groups of workmen was (November, 1923) 53% of the 1913 wages and the wholesale trade index figures of prices at the same time showed 139% as compared with 1913. That is, the man who was lucky enough to have a job received a little more than half of what he would have received in 1913 and had to pay 40% more for

the necessities of life. This produced very great hardships, but now prices are falling rapidly and are probably about 112% of the 1913 range. The wages of all the groups reported as late as December showed marked increase and justify the statement that they are now (February fifth) nearly, if not quite 80% of the 1913 rate of wages. With wages 20% less and prices 12% higher than in 1913, they may not be said to be prosperous, but they buy less. They have learned a lesson in economy, and unless another calamity intervenes, their condition will improve.

It is interesting to speculate upon the probable effect of these experiences upon the thrift and industry of the people. The first impulse to spend money as quickly as possible in order to escape loss from its depreciation must have induced great extravagance and waste, but the later experience of being forced to get along without income and in a period of high prices must have had the effect of forcing the most rigid economy. The great expenditure of those whose speculations had made them rich, has probably been productive of as much resentment at home against extravagant expenditure, as it has of suspicion abroad of the existence of great amounts of concealed wealth in Germany.

The country has gone through every stage of the experience of inflation, the first steps of which are always so intoxicatingly pleasant—the rising prices and wages, the great activity of exchanges and the pleasure of perceiving that the hated creditor class was being hurt and that debts were more easily dis-

charged. Such things made every German feel sure that his country was being brought through great difficulties with great skill. But the later effects were as disagreeable as the first were pleasant—the lack of work, the scarcity of money and later the scarcity of food and all materials, the tragical injustice of the enforced expropriation of property and the biting poverty of the great majority of the people. These things have really shaken the confidence of the people in the wisdom of the government. Some of those who have been in Germany a great deal in these recent years say that they believe the people generally would actually welcome the appearance of outside coercion upon their government.

It is apparent from the expressions of Doctor Schacht that he, and probably the most intelligent Germans, were surprised at the general acceptance of the Rentenmark by the people generally and the agricultural interests in particular. The degree of stabilization of currency so quickly accomplished was utilized by the government for the improvement of its revenues. The management of the national budget during a period of depreciating currency presents insurmountable difficulties. Future requirements of the number of marks required to accomplish certain results can not be calculated unless the future value of the mark be known; and taxes that are assessed when the mark has a certain value are collected when that value is much reduced. So that it is no wonder that the revenues of the government and of the railways were entirely insuf-

ficient during this period of inflation. Upon the reappearance of stability, however, immediate measures were taken to provide sufficient income for the state.

The whole taxation system has been revised. The Weimar Constitution conferred upon the Reich "the legislation in respect of revenues in so far as totally or partially they are claimed or utilized for its purposes,"—this is quoted from a translation of the statement submitted by the German Government to this Committee,—"and furthermore a right of establishing principles concerning the admissibility and the mode of collection of state taxes and duties. As for the repartition of fiscal sovereignty between the Reich and the component states, this problem was settled by the *Landessteuergesetz* (fiscal state legislation) of March 30, 1920. By virtue of this legislation, the states and communities are entitled to collect taxes, pursuant to their respective home legislation (*Landesricht*) in so far as this is not in contradiction with the Reich's legislation. The levying of taxes by the Reich excludes the possibility for the communities of levying in their turn identical taxes. The collection of any supplementary taxes to Reich's taxation is illicit, unless a special authorization by a Reich enactment has been granted. The principal taxes left to the states are taxes upon landed property and licenses. The communities are bidden to collect a tax on entertainments. By way of compensation for the income tax, the states and communities receive by retrocession certain quotas amounting at first on

income tax to two-thirds; in the case of the inheritance tax to one-fifth; in that of real estate to one-half; and in that of the tax on turnover to one-tenth for the states and one-twentieth for the communities. These proportions were increased by supplemental legislation of June 23, 1923, to meet emergency caused by the falling mark."

It seems to be almost impossible to form any definite conclusions from the study of taxation, revenue and government expenditure in Germany during 1923, the year of the great inflation. Some severe criticism has been made of the mildness of taxes and the foolish inadequacy of railroad rates. How under the circumstances it could have been otherwise to outward appearances, or how any sane system could have been applied to such conditions, it is difficult to see. At the present moment, however, and since December 19, 1923, the charge of shirking the burdens of taxation can not be made against the German Government. Indeed it would appear that the accusation might be that their effort just at the moment is to extract too much. A lower rate of taxation in some cases would produce greater revenue. In our own country we shrink from a tax on sales, even of 1%. In the second emergency decree of December, 1923, there was established in Germany a tax on turnover, or sales tax, of 2½% augmented by a tax of 15% on special goods of luxury and a tax of 5% and 10% for services of a special kind, such as hotels, advertisements, etc.; also substantial taxes on sale of real estate, on the organization of companies, on the sale of stocks and bonds,

on directors' fees (20%); on automobiles and carriages; on railroad fares and freight charges; on betting (10% of amount wagered for) and on lotteries (20%); on tobacco, beer, wine, sugar, matches, etc.; and in addition to these and others, a tax on incomes, 10% (fifty marks a month exempted) on wages and salaries, and on the total income of 10% of the revenue from fixed investments, and if the income exceed two thousand marks per quarter year, 20% on salaries and wages.

Of course this is not an attempt to outline a taxation system. It is enough to show that there is now a serious attitude toward the subject of taxation. Large revenues must be raised in addition to these taxes by the cities and states, but these share in the proceeds of the Reich's taxation. The turnover tax of 2½% augmented by the income tax and the special taxes might prove to be destructive of revenue and of business too, if the ideas prevalent in America about the sales tax are sound. These taxes are burdensome enough but whether they will produce the revenue is another question. It would seem that the system was hastily organized and probably ought to be altered soon.

The business turnover tax in France is 1% plus one-tenth for the benefit of departments and cities, and produces more revenue than the income tax, which is levied upon all incomes in excess of seven thousand francs (now about three hundred fifty dollars); it begins at 4% and increases rapidly with the increasing size of the income. Upon an income of eight thousand dollars the tax is about 25% and

FIRST COMMITTEE IN SESSION AT BERLIN

Left to Right, Sitting: FLORA, ALLIX, PARMENTIER, DAWES, YOUNG, KINDERSLEY, STAMP, FRANCQUI, HOUTART; *Standing:* SECRETARY MACFADYEAN, DENIS, MATTHIEU

NEWSPAPER PHOTOGRAPHERS IN BERLIN

upon an income of twenty-five thousand dollars about 60%, and of course more on larger incomes. In addition, the stamp and registration taxes produce large revenues—in 1922 a little more than either the turnover or the income tax. There was also a tax levied on war profits graduated and varying from 50% to 80% upon profits earned between August, 1914, and June 30, 1920, which up to quite recently was very productive, and heavy taxes upon consumption, upon monopolies, upon customs, etc., an appalling list; and just now they are passing legislation adding 20% to all these taxes. Except as to the gross sales or turnover tax, the French system appears the more burdensome, but comparison is difficult.

Berlin, February 8, 1924.

Doctor Schacht made an address yesterday at Koningsberg in which he declared no other state ever had such taxation burdens as Germany. "Such burdens are possible only temporarily, and during a transition period and this is especially in view of the loss of working capital through currency inflation and the collapse of the formerly highly developed cooperative organization."

In the figures just furnished of estimates for the budget of 1924, they estimate the proceeds of the turnover tax (augmented) at about one billion, four hundred million gold marks, of which two hundred fifteen million goes to the states; the proceeds of the income tax at about one billion four hundred eighty-eight million marks, of which one billion

three hundred thirty-nine million goes to the states; the estimated returns from passenger and foreign taxes were two hundred thirty million; from racing bets forty million; from tobacco three hundred sixty million, etc., and from customs only one hundred sixty million. The total estimated receipts for 1924 are five billion one hundred forty-four million gold marks, which except for reparations and the expenses connected therewith, is deemed sufficient to meet their expenses. This would be probably about 80% of the taxes collected for the same purposes before the war, and this fact, in view of their present condition and past experiences, together with the nature and extent of the taxes themselves as fixed in December, are indicative of a realization on the part of the German Government of the necessity of severe and rigid taxation and of their confidence in the recuperative powers of the nation.

The recovery of Austria from conditions even worse and in the face of obstacles at least as great, ought to give great encouragement to this confidence.

The organization of a bank of issue was the main feature of the reconstruction work being accomplished in Austria under the auspices of the League of Nations. This bank was opened on January 1, 1922. The following statement of results anticipated and those achieved has been submitted to the Committee:

The League scheme aimed at immediate and complete stabilization of the crown; and at a reform of the budget resulting in stable equilibrium at the end of 1924. The deficits till that

date were to be met from the proceeds of an external loan amounting (net) to about twenty million pounds secured by international guarantees and certain Austrian gages. The progress may be conveniently shown in the following tabular comparison:

League Anticipation	*Result*
1. Value of the crown to be maintained stable.	Fully achieved. Value Jan. 1922, $\frac{1}{14272}$ of gold value. Value August, 1923, to January, 1924, $\frac{1}{14298}$ of gold value without variation. This exchange value has been maintained in spite of an increase in note issue from 1,517 in September, 1922, to 7,126 milliards in December, 1923. The cover amounts to 55% of issue and 100% cover is being retained for new issues. The difficulty is to avoid *appreciation* without giving the country more currency than it needs and so raising internal prices.
2. £20,000,000 provided for 2 years budget deficits. It was contemplated that the greater part of this would be spent in the first year.	£9,000,000 only has been spent in the 13 months January, 1922, to January, 1923, inclusive.
3. Equilibrium on a stable basis was to be attained by December, 1924.	Taxation receipts equaled expenditure in January, 1924. This may be only a temporary equilibrium. It is due to a great rise in receipts (due to a prosperity of which some of the causes are temporary), not to a reduction in expenditure.
4. Taxation was estimated to average per month for 1923, first half-year 26.5 million g. c.; second half-year 31.4 million g. c. No attempt was made to form close estimates. It was thought more prudent to work on a maximum expenditure basis. No great importance should therefore be attached to above figures.	Average first half-year, 1923, 35.1. Average July-October, 1923, 35.8.

5. Expenditure. Was to be gradually reduced to a basis of 350 million g. c. a year or 29.2 million g. c. per month by the end of 1924.	Changes in accounting arrangements make a precise comparison of results with monthly statements difficult. The closed accounts for the first six months of 1923 show an average monthly expenditure of 49.4 million g. c. and for July-October, 1923, of 42.4 million g. c. The rate of reduction would require to be increased in order to come down to 29.2 by December next.
6. Dismissals of personnel. 25,000 to be dismissed by January, 1923. 50,000 to be dismissed by July, 1923. 75,000 to be dismissed by January, 1924. 100,000 to be dismissed by July, 1924.	By January, 1923—23,641 By July, 1923—45,030 By January, 1924—61,204
7. Assigned revenues. Customs and tobacco receipts. The customs plus net tobacco receipts were estimated at 6.6 million g. c. per month. (The gross tobacco receipts are technically taken as gage but it was thought more prudent to base estimates on net yield.)	The actual customs plus net tobacco receipts average per month— In first six months of 1923, 8.9 million g. c. July-October, 1923, 12.6 million g. c. The gross receipts of customs and tobacco average per month In first six months of 1923, 13.1 million g. c. In second six months of 1923, 18.6 million g. c. In January, 1924, 24.5 million g. c.
8. Unemployment. Expected to be serious, but no precise estimates made.	The numbers of unemployed at different months were: September, 1922 ..... 38,000 January, 1923 .....117,144 March, 1923 .....167,417 May, 1923 132,226

July, 1923	92,789
September, 1923	83,891
November, 1923	75,780
December, 1923	77,782
January, 1924	95,069

There was therefore a serious figure in March, 1923. This, was, however, never so serious a percentage as in Great Britain, Czecho-Slovakia or Switzerland and was rapidly reduced. The latest figures again give cause for anxiety.

Other Statistics 1923

Commerce	Jan.	Mar.	May	July	Sept.	Nov.
Value of Imports (millions g. c.)	90	143	98	123	138	169
Value of Exports (millions g. c.)	59	79	71	77	80	84
Adverse (visible) trade balance	31	64	27	46	58	85

These figures are more important as showing the expanding economic activity in Austria than as suggesting a serious adverse balance. The "invisible exports"—for which no exact estimates are available—are a very large factor and the "invisible imports" are not of a corresponding importance. A *visible* adverse balance in fact only reflects the fact that Austria is largely dependent upon the financial earnings of Vienna.

Financial Statistics	Jan.	Mar.	May	July	Sept.	Nov.	Dec.
Note circulation (milliards g. c.)	4,110	4,459	4,837	5,684	6,225	6,578	7,126
Obligations to be met at sight (milliards g. c.)	279	329	343	535	374	617	649
Reserve in gold and foreign exchange (milliards g. c.)	1,108	1,422	1,756	3,020	3,200	3,567	3,915
Percentage of reserve for note circulation and obligations at sight	25.2	29.7	33.9	48.6	48.5	49.6	50.4
Value of note circulation in gold crowns	285	309	336	394	432	456	495
Savings at chief Joint Stock Banks and Savings Banks in millions of gold crowns	7.7	13.3	18.1	23.5	30	35.1	38.2

Index figures (in September, 1922, the savings were only two million g. c. so that they increased twenty-fold in 16 months).

CHAPTER IV

COMMENSURATE BURDEN OF TAXATION IN GERMANY—EFFECT OF DEPRECIATION OF THE MARK—PORTION OF BURDEN OF REPARATION PAYMENTS TO BE BORNE BY RAILWAYS AND PRIVATE INDUSTRIES—CONSIDERATION OF NEW BANK OF ISSUE—TRANSFER OF PAYMENTS ON REPARATIONS TO CREDITORS—EFFECT OF REPARATION PAYMENTS ON CURRENCY STABILITY—MEMORANDA BY EXPERTS ON PROBABLE RESULTS FROM "GOLD STANDARD"—HOPE OF SOLUTION UPON LEAVING BERLIN.

Many of those who had followed the previous discussions about the reparation problem probably expected that this Committee would become involved at once in a discussion of the aggregate charge to be laid upon Germany and would regard the definite fixing of this sum as the very first step toward balancing of the budget. That might have been necessary had a definite burden ever been laid upon and exacted from Germany, or at least any such burden as one hundred thirty-two billion marks. Even upon the fifty billion A and B bonds, definitely issued and delivered to the respective creditors of Germany, no regular payment of interest has been made. Payments have been made but not enough to cover the full interest charges. The C bonds were never issued; the conditions under which they might be

issued have never been realized. The issuance of the A and B bonds was a device by which there was created a very definite acknowledgment of a continuing obligation; they provided what might have been considered as a convenient accounting method. But if it was ever expected that they would be useful in securing immediate funds by being sold to private investors, or that they would prove of value in clarifying the situation, such expectations have not been fulfilled. They have rather served to obscure the truth that the real demands made upon Germany were for annual payments and for such payments as could be made from the proceeds of taxation in Germany, equal to that borne by her creditors.

In July, 1921, the Reparation Commission fixed these payments at two billion marks a year, plus 26% of exports. This amount was not interest on one hundred thirty-two billion marks, it bore no relation to interest charges, but it was more than Germany has actually paid. The Committee has found it no more necessary than the Reparation Commission did to assume the task of fixing definitely the ultimate capacity of Germany to pay. It takes the situation as it exists, submits a plan which in its judgment will develop Germany's capacity to pay more than she could pay in the lack of such a plan. If after a few years these payments suffice to meet the charges upon the A and B bonds outstanding, then the payments may be distributed according to the ownership of those bonds. If fortunately there should be an excess, some portion

of the C bonds might be issued, or some entirely new method of acknowledging the obligation employed. Having agreed that Germany ought to bear equally with its creditors the burdens of reconstruction and that as nearly as could be determined she ought to be taxed as heavily as the nations which accepted her challenge and defeated her purpose, they have avoided the fixing of Germany's ultimate burden and have not even discussed it as a subject-matter within their province. The settlement of this rests with powers signatory to the Treaty.

But all the time every member of the Committee has known that there were two very difficult and important questions that must be faced; first, by what test could the Reparation Commission "satisfy itself that in general the German scheme of taxation is fully as heavy as that of any of the powers represented on the Commission," as they were bidden by the Treaty to do? And, second, having fixed this, what limitation, if any, ought to be fixed upon the payments to be made outside of Germany?

In answering these questions the Committee will face the same difficulties that have perplexed the Reparation Commission. In estimating what constitutes a burden, there are many things to be considered that do not appear upon the surface.

In the first place, it is necessary for purposes of comparison to reduce the debts of all nations to some common currency. The franc as measured by its purchasing power to-day is probably worth nine cents; its foreign exchange value is less than five cents. The total indebtedness of France is about

four hundred fifty billion francs; at the old parity, this would be about ninety billion dollars; measured by the present purchasing power of the franc within France, it would be about thirty-eight billion dollars and measured by the foreign exchange value of the franc (its purchasing power abroad) it would be about twenty-two billion dollars. Even these results would require amendment owing to the fact that some of the aggregate of France's indebtedness is payable in dollars and pounds. The real weight of the debt, however, is actually determined by the average value of the currency during the whole period of paying the interest and the principal. If in the case of France large collections should be made from Germany, the franc might rise. If it should, its debt measured in dollars would grow very rapidly, even though outstanding bonds had been retired by the proceeds of the collection.

This is one of the difficulties. Another is introduced when it is assumed that the burden placed upon Germany will create a credit in the Allied nations, which ought to be deducted from the debts of these nations at the present foreign exchange values.

Moreover, the burdensomeness of a debt is related to the wealth of a nation and the gross income of its people. A debt of a certain amount per capita upon Germany and the United States would not be equally burdensome. An equal amount of debt produces an unequal burden, because of the greater wealth per capita in the United States.

Furthermore, the burden of taxation is divided in some nations between states and federal government and in other nations it is not, at least to the same degree. The per capita taxation in Illinois is forty dollars for state and local purposes and about thirty dollars per capita for the Federal Government. For purposes of comparison in Europe thirty dollars is considered our burden of taxation, but in Chicago it is not so considered. Another consideration, which many think can not be overlooked, is that as taxes must be paid from the surplus of income over expenditures, there must be some study of the minimum cost of existence in the various countries. As taxes are a necessary part of the cost of living (since in civilized life, sanitation and policing at least are required), there must be some consideration also of the scope of taxation in different nations. In all countries some of the necessities of family life are furnished by the state but more in some than in others, and the cost of maintaining a family is reduced in proportion as necessities are supplied from the proceeds of taxation.

Another factor of great importance not often mentioned must undoubtedly be considered in connection with this problem, namely that the process of inflation has extinguished internal indebtedness in Germany. About ninety billion marks due from the government of Germany to its own people was wiped out by inflation. It can hardly be said that after this process there was only a clean sheet left. It is true there was no physical property destroyed, only personal property, but to the extent of about

fifteen hundred marks per capita the individual German had suffered the destruction of savings invested in national bonds. He had lost his working capital and undoubtedly had suffered a diminution of his ability to pay. So far as he is personally concerned, he feels he has already paid the costs of the war, and if there is not some element of truth in this view of the case, then it would be perfectly easy for France, through inflation, to wipe out her own internal indebtedness and thus free herself from burden.

These and probably other serious difficulties are encountered in the effort to establish a commensurate burden of taxation in different nations upon the assumption that in all these nations the entire proceeds of the taxes are to be expended within the country and for the satisfaction of some real need or desire of the taxpayers themselves. Under these circumstances the money remains in the country; it is collected from the people and being expended is distributed among them and to a great extent revivifies their ability to continue the process. If bonds are outstanding, the people as taxpayers provide the funds to pay to themselves as bond-holders. It necessarily lays a burden of unequal weight upon different individuals but in the aggregate no national resources are directly reduced; the aggregate wealth and the gross current income of the nation remain almost unchanged. But when the proceeds of taxation are to be paid outside of the nation itself, there is necessarily an exhaustion of resources and a draft upon national wealth and income. This

is true whether the payment is made at the time the taxes are collected or deferred. This creates a double strain, one upon the economic resources of a country and another upon the sentiment of the taxpayer. The former is sufficiently apparent to have attracted wide attention; the latter also must be taken into consideration.

Men who spend lavishly in entertainment, groan piteously in the payment of taxes, but their spirit may be consoled by the contemplation of personal or social benefits received in compensation. If money is extorted from them in the payment of taxes, a compensation is received in personal or community benefits brought about by the expenditure of the proceeds of taxation—sewers are maintained or the supply of water, roads are kept in good condition, schools are established and the poor and needy, sick and afflicted may be relieved. These are personal and community advantages in which every taxpayer participates. Such things tend to lighten the burdens of paying taxes. When, however, a portion of the taxes collected is sent outside of the country and no direct and immediate benefit can be felt, the sense of injury and oppression in connection with the payment of taxes is greatly aggravated. It adds to the burden.

In any case, when the war was started, it became inevitable that in the defeated countries, the moral strain of making payments to some extent in foreign currencies would have to be endured, and this aspect of the question must not be stressed too much. In view of the fact, however, that these payments

must extend over a period of years, some consideration must be given to the moral as well as to the economic strain of making payments in foreign exchange. The strain must not be permitted to reach the breaking point. The capacity to pay must be measured by conditions, and requirements which might reduce capacity to pay must not be enforced.

Taking into consideration all of these and other complications, it is to be doubted if any economists could produce a definite table of commensurate burden that would be accepted by any other economist.

One of the members of the Committee has just submitted a study of this problem but without detailed discussion of the theories adopted. He begins by stating that Germany had a burden of about five billion gold marks per year as a debt service charge at the end of the war as interest upon her own internal debt, of which she was relieved by inflation; then computing the indebtedness of Belgium, France, Great Britain and Italy upon a gold exchange basis, he concludes that if Germany were to carry a debt upon the same scale as these other nations, that debt would be expressed in millions of gold marks.

64,021	as	the	equivalent	of	the	Belgian debt
106,404	"	"	"	"	"	French debt
216,600	"	"	"	"	"	English debt
29,264	"	"	"	"	"	Italian debt

Her interest charges if the per capita indebtedness were equal to that of Great Britain would be

eleven billion gold marks. If the per capita indebtedness of Germany were equal to the average of the four Allies, the interest on it would be about six billion gold marks. "It will be seen, therefore, that by the test of the Germans' own debt or of that actually being borne by her victors, the German people should be taxed to the extent of at least five or six billion marks in addition to their own administrative expenditures." But if the comparison be made upon the national and local taxation borne by Great Britain for example, an equivalent burden for Germany would be twenty-four and eight-tenth billion gold marks. "But a very large part of the taxation of the United Kingdom is raised for the purpose of paying interest and the sinking fund to her own nationals and, therefore, returns to them as income. In a narrow sense although a burden on particular taxpayers, it is not a burden on the country as a whole."

He next asserts that it will be said that a mere per capita comparison, irrespective of average wealth, is impossible or misleading. At the period of her greatest development, the per capita income in Germany was 60% of that in Great Britain. Taking this into consideration and the greater ease of paying interest on internal bonds, he considered that nine billion marks might be regarded as a commensurate burden for Germany, as compared with England, and states that similar figures would be supplied for comparison with the other Allies. It is rather hoped that the conclusion of the Committee, assuming they pursue this study, will be announced without a confusing discussion of the

method of reaching it. There would be more agreement as to the amount than as to the method of computing it.

The burden of obligation created by the war has condemned the people of all the Allied Nations to the payment of the maximum of taxes which can be borne without destroying the incentive to continued and increased production. Since the creditors of Germany are paying taxes to the utmost limit of their capacity, the application of this rule of equality in the burden of taxation must certainly mean that Germany also must pay taxes from year to year to the utmost limit of her capacity. More than this could never be extracted; less than this would relieve Germany from the common hardship. And this is not by any means inflicting a penalty; it is rather distributing the burden.

The system of taxation established in one nation as being that which would produce the maximum of revenue, without destructive effect at a particular time, might, if transferred and applied to the people of another nation, at the same time, result in comparatively low revenues, in disturbed conditions of business and even in distress that might lead to emigration. Some modified scale of taxation, adjusted to the conditions existing in the country in which it is applied, would not only produce greater revenue, but would maintain and increase production, whereby the capacity for later tax payments is sustained. Any taxation which diminishes materially the capacity to produce, reduces in the same measure the ultimate capacity to pay taxes.

In considering a scheme of taxation in Germany

that shall be as heavy proportionately as that borne by other nations, it is, therefore, not so important to measure schedules item by item, as it is to make certain that a system be established calculated to secure the maximum of revenue without the destruction of productive power. In a practical way equality in the burden as between two nations, is established when both nations are being taxed upon this basis.

Yesterday Mr. Kemmerer submitted a suggestion, which may change the method of attacking the problem. Its simplicity commends it and all of our experts have endorsed it as worthy of careful study and more likely to lead to good results than any suggestion heretofore made in this connection.

A Possible Alternative Plan

Require Germany to pay to the Allies annually for a fixed period of years an amount representing a definite percentage, for example, 20% or 25% of her national and state revenues. If preferred, payments could be made annually for an indefinite period of years until a predetermined sum, principal and interest, has been paid. These annual payments might be in lieu of all other reparation payments or they might be supplemented by one or more other payments, as for example, a payment in the form of railway bonds.

Among the merits of this plan the following may be mentioned:

First: The plan makes the motives of the Ger-

mans and of the Allied people move concurrently instead of in opposite directions. The more Germany prospers, the more she will be able to pay and the larger will be the reparations the Allies will receive. It will be to the interest of the Allies, therefore, to see Germany prosperous.

Second: The uncertainties in connection with reparation payments arising from fluctuations in the value of gold, in terms of which amounts are stated, would be eliminated. By the plan proposed, if the value of gold should decline (*i. e.* the price level should rise), Germany's revenue receipts would likewise rise; and if the value of gold should rise (*i. e.* the price level fall), Germany's revenue receipts would tend downward, so that in either case the amounts payable to the Allies would vary with the value of the money paid.

Third: Inasmuch as Germany would herself receive the major part of revenues collected and as her officials would be publicly responsible to her people for the expenditures of these revenues, there would be strong public pressure for honesty in making collections and keeping accounts.

Fourth: The plan gives Germany the maximum degree of freedom in working out her own tax and revenue program (gages, if thought necessary, could of course be taken on this plan as well as on any other).

Fifth: The plan has the merit of great simplicity. The man in the street can not understand "commensurate burden" but he can understand "twenty cents on the dollar."

But nevertheless, even though the discussion of the methods for ascertaining it may be avoided, it is not likely that the basis of commensurate burden for the ultimate settlement can be abandoned. It furnishes a moral principle which all must recognize. No man can question the justice of equalizing the burden of the war. To deny it would be to set up the absurd claim that Germany alone among the nations was without fault in beginning and conducting the war and that she must be rewarded for her defeat by tremendous advantages at the expense of the Allied Nations.

The Belgian proposals, submitted by Monsieur Francqui, are being considered. As they are quite long and poorly translated, a condensed statement of them is made. The opening statement is that the restoration of German economic life must be dealt with from every aspect. Germany must be enabled to distribute reasonable payments among its creditors in order to meet the difficulties and in some cases the otherwise inextricable difficulties faced by these creditors, and this upon a permanent basis, which implies due regard to the welfare of the creditor nations, for their collapse would destroy Germany. In the near future there probably will be a surplus of German revenues even without the railroads, which will soon yield large profits. Under what circumstances and how can this surplus be paid into the reparation fund for distribution? He then quotes from Sir Josiah Stamp (without including his full discussion which qualified this statement) to the effect that Germany could soon raise

Monsieur Emile Francqui
Belgian Member First Committee of Experts

eleven and one-half billion marks revenue and have available for reparations four and one-half billions. To provide that this be done would require dangerous interference in the internal affairs of Germany. Other means must be found. Particularly because a control over the disposition of revenues would not presumably be effective in preventing the dumping of German goods on the international markets. Therefore, there ought to be eliminated from the German budget the receipts which can be easily controlled.

He refers to railway receipts and the various taxes on consumption dealt with in the Belgian study, which, he states, the German Government has favorably received.

An organization ought to be created to demand from German manufacturers a portion of the profits realized from 1913 onward, especially those made by the automatic cancellation of their debts brought about by the collapse of the mark. The appropriation to the reparation fund of railway profits, monopoly receipts and levies on fortunes abnormally acquired through the fall of the mark, does in fact chiefly affect those members of the community whose capital has been abnormally augmented.

Could not the Committee suggest the organization of a private company to operate such monopolies as alcohol, tobacco and beverages under the same system of control as that applied to the Bank of Issue? It is certain that the German Government would as readily agree to the control of these monopolies as they have to the international control of the

bank. The German Government has already indicated its intention to operate the railroads through a corporation upon a profit earning basis and the organization of a company under international superivision would be in conformity with their plans.

Let the German Government receive all the ordinary shares in such a company, and let from one hundred million to one hundred fifty million gold mark issue of preferred shares be made to be subscribed by individuals within and outside of Germany for working capital. The company would be placed under the direction of a board of managers, consisting of Germans and foreigners in equal numbers, the chairman to be a German and one of the foreign directors to be entrusted with the duties of a comptroller, who would particularly see that rates are fully applied in such a way as to make dumping (through freight rebates) impossible. The company would issue a certain number of bonds, the proceeds of which would be assigned for reparations; after payment of interest on the bonds, a moderate rate to be paid on the preferred shares and the surplus divided between the preferred and ordinary shares in some ratio to be determined later; and a similar system might be adopted in connection with the monopolies. At the close of his discussion he outlines this arrangement, which presumably applies to the railroads also. "The trustee accountant will only be authorized to issue to the public a nominal amount of bonds, determined by the ratio of two-thirds between interest on bonds outstanding and net earn-

ings of the company. The duration of concessions of monopolies to these companies to be, for instance, thirty-seven years. Each monopoly to issue bonds and if these bonds were not retired out of earnings within that time, the period of concession to be extended. On the other hand the German Government will have, after the tenth year, the right to terminate concessions by paying off the bonds in a lump sum. This whole system to be directed by two trustees, a trustee cashier, who would be especially entrusted with the movement of currencies of all the companies, and a trustee accountant, who would be concerned "with the movement of the bills of all the *régies*" (monopolies or controls). All these companies to be inseparable parts of a whole of which the proposed bank of issue is the base. Any deficiencies of earnings below interest of one would be made up from the surplus of the others.

"Whatever moderation may be shown in fixing immediate payments, there is one guarantee which can not be forgotten, the immediate organization of means to insure future payments, *i. e.*, the immediate application of the measures sketched out above for placing in the hands of the Allies a reliable pledge for the payments expected from Germany."

Monday, February 11, 1924.

Our stay in Berlin is drawing to its end. We shall leave on Wednesday. The government had taken pains to prepare in advance information and to furnish it as promptly and exactly as possible. As

for ourselves, Ambassador Houghton has on several occasions been our most agreeable host, and in every way both by advice and by introductions to Mr. Young has been very useful indeed. We have seen some very fine operatic performances as his guests, and we have on our own account not failed to visit the public kitchens and relief stations where the poor are being fed. The general method of this work pleased us in all particulars.

The *Berlin Tageblatt* printed a little article on February seventh, which tells about the offices put at the disposal of the Committee:

How the Experts Work

9 Bellevuestrasse: From the noisy Potsdamer Platz you enter this once aristocratic street, where the dwellings have been replaced by offices. Walking past the Esplanade Hotel, you find between houses a thoroughfare with a few columns indicating that here begins one of those private streets frequently to be found in the Tiergarten quarter. Between the columns there hangs a regular sign-board *Reichswirtschaftsrat*—black upon white, not at all official. The thoroughfare ends in a lawn grown with old trees, and on it is built a large box, the house of the *Reichswirtschaftsrat* in which the experts will be residing for some weeks.

Formerly it was called *Konigliches Wilhelm-Gymnasium* (grammar school), which has ceased to exist for some months. Only the head-master is still living in his old-fashioned house lying opposite the school. A monument of the old emperor is still there, too, but one feels that one does not longer know why it is there. The weather is too cold; otherwise one might see the experts taking their

ease, during the sitting intervals, on the stone benches of the monument.

When the house was rebuilt for the *Reichswirtschaftsrat,* many things were altered, but—to tell the truth—a last remainder of school-atmosphere was not wholly expelled. There is still a smell of class work. In the entrance hall, we are welcomed by Sophocles; on the left and on the right, there are two corridors, and then—another world. On the door we read names which mean more to mankind to-day: Young, Parmentier, Pirelli—the rooms of the experts. A room has been placed at the disposal of each expert; on the ground-floor there are the Frenchmen and the Americans; on the first floor are the Englishmen, the Italians and the Belgians, on the second there is the chief secretary office. Mr. MacFadyean, Chief Secretary of the Reparation Commission, has taken the management of the offices into his hands and commands a numerous auxiliary troop of technical officials, interpreters and lady typewriters, also two American professors, statisticians and experts in bookkeeping. A prodigy of an interpreter, Paul Mantoux, who worked at the Peace Conference and was then appointed department chief of the secretary office of the League of Nations, is not among the interpreters, but in return for this, we can show at least one talent, the interpreter of the War Cost Commission—Michaelis, who masters ten languages and has been present at all the great international conferences: Versailles, Brussels, Cannes and Genoa. The interpreters, by the way, have important services to render, for their help is used also for the conversations among the experts themselves. McKenna, for instance, does not speak French. The work is, of course, considerably simplified, if the assistance of interpreters is not needed. We well remember what impression it made when Walter Rathenau repeated his speech himself in English and French.

A similar impression has been produced on the experts when they saw that several German referees, such as Bergmann and Doctor Schacht, could answer to English and French questions in the same language so that the interpreter had to translate into one language only.

With very few exceptions, the sittings take place in the rooms of the experts, those of the First Committee in Mr. Young's room, those of the Second Committee in Mr. Atthalin's room, even if German referees are consulted. There is no pomp, no ceremony on the whole; no chairman, no standing orders. They are sitting round the table smoking cigars or cigarettes. General Dawes, of course, smokes his pipe and speaks to the point. There is also a sitting-room which is, however, seldom used. In former times it was the lower fourth form of the grammar school; now it hears things more important than the mysteries of the Greek verbs ending in "mi."

Doctor Meyer, who keeps the experts in touch with the War Cost Commission, is in a room which was the ancient preparatory class, where he had once been himself when a boy. The experts apply to him with all their requests and he, then, gives his orders, which are not always easy. It was also he who received the two committees at the station.

Some of the experts know Berlin from former visits; one even attended the lectures of the university and speaks with veneration of Schmoller and Wagner. Atthalin was here several times, also McKenna. Both committees reside at the Esplanade Hotel. By the way, it is interesting that the Americans, also, in formal things lay stress on their non-cooperation in the Reparation Commission. They pay for their stay themselves, whereas else the Reparation Commission defrays the expenses. As, however, the Reparation Commission is paid by ourselves, Germany profits a little by the manner

of accentuating the line of demarcation and we are thankful for that, even if it is meant otherwise. We should, however, be more delighted to have seen the Americans from the very beginning in the Reparation Commission; Europe would then look quite different. In the hotel, the experts lead a very retired life, only the chief secretary and the Belgian Francqui have taken their wives with them. Things have changed since that first visit of the Reparation Commission. It was the time of the beginning fall of the mark which caused the prices of German articles to go down considerably and foreigners came in troops to Germany and bought whatever they could. Then a member was considerably late at a sitting in Wilhelmstreet and made his excuse by saying that he had been shopping "pour participer a l'Ausverkauf" [in order to profit by the bargain sale of Germany].

The Banking Committee has been devoting much study to the preparation of the plan for the new bank. This new bank of issue is designed to be the essential agency for creating in Germany a unified, stable and elastic currency, which will provide a sound basis for domestic credit, facilitate the balancing of the budget and provide for the discharge of its external obligations. The full attainment of this purpose will promote the stabilization of other European currencies and the resumption of normal trade relations between the nations of Europe. The temporary stability of the currency now prevailing will facilitate the accomplishment of this plan, and it is highly important to have the organization completed and the bank in operation before any disturbance of present conditions occurs. They have

worked out an arrangement whereby the new bank shall be organized under a charter of fifty years' duration with a capital of four hundred million gold marks and of this capital one hundred million marks may be used to acquire the property of or to merge with the Reichsbank. The bank will be managed by a Board of Managers, all of whom are to be of German nationality and to be selected by the president of the bank, and presumably from the staff of vice-presidents. This board will direct the discount and credit policy of the bank, fix rates of interest and draft regulations of policy. The General Board of Directors shall consist of fourteen members, one-half of whom shall be foreign and one-half of German nationality. The foreign members of the first General Board shall be appointed by an organization committee composed of the president of the Reichsbank and one member of the Committee of Experts, and the Board in filling vacancies in the future shall consult with reference to such election the central Bank of Issue or any financial authority of the country, whose citizen is to be chosen, but citizens of the following nations are eligible: England, France, Belgium, United States, Holland and Switzerland. By unanimous vote the number of German members of the Board may be increased. A commissioner shall be appointed who shall be a foreigner to be elected by a majority vote of not less than nine members of the General Board of which majority six shall be of foreign members, whose duty it shall be to enforce the provisions of the law relative to the issue of notes and main-

tenance of the bank's reserves. The power of the bank to make loans to the government is strictly limited and subject to the control of the General, as distinguished from the Managing, Board. The bank shall have the exclusive privilege of issuing circulating bank-notes as legal tender money, but all of the conditions controlling this feature of its functioning have not yet been determined. There is also included in the plan an arrangement for supporting and at some later time retiring the Rentenmarks in circulation, as well as for providing for the permanent stabilization of the Reichsmark at the ratio of a trillion to one gold mark.

In general it is proposed to establish this bank upon a gold exchange basis as securely as existing conditions and future fears will permit. As to the exact restrictions by which this is to be accomplished, there is much difference of opinion, but the final conclusion of their discussions may be found in Annex No. 1, the Plan of the Bank as finally submitted.

All of the members of the Banking Committee are devoting much labor to the task of preparing these plans. Sir Robert M. Kindersley applies himself to this work with indefatigable industry. His long experience in banking, his painstaking accuracy and unassuming but great ability, make his contributions to the completion of this work invaluable. The president of the great banking firm of Lazard Freres, a director of the Bank of England and the chairman of the Board of Directors of the Hudson Bay Company, Sir Robert brings to this work the

lessons of a wide experience. Mr. Henry M. Robinson, the American member of the Second Committee, has been invited to sit with this Banking Committee and thus has the unique experience of serving actively on both Committees. His intimate knowledge of the technical features of banking and his education in and the long practice of law, enable him to be of the greatest service, and the value of his contributions is cordially recognized by all. The Belgian member, Monsieur Émile Francqui, is a man who has had a remarkable and varied life in the development of the Belgian Congo, in the building of railroads in China, in the production of radium, in banking and in the political life of Belgium. He understands well the theories of economists and tempers every discussion with the highly practical suggestions of a widely experienced business man. Like Sir Josiah Stamp and Sir Robert Kindersley, Monsieur Francqui is untiring in his industry. The French member, Monsieur Parmentier, has gained the admiration and respect of all the members of the Committee, both by reason of his thorough technical knowledge and his excellent judgment and tactful conduct. Doctor Alberto Pirelli, the Italian member, is the head of one of the greatest industries of Italy, and a man of sound judgment and wide knowledge. It is impossible to believe that any men could be found better qualified by ability, experience, knowledge and judgment, to do this particular work than these very men appear to be. There seems always to be a mutual respect between them, and a cordial cooperation in their common

task. Mr. Owen D. Young is chairman of the Committee, and has gained the admiration and esteem of its members in the same degree as he had already won that of all the Americans engaged in this work.

There have been conferences between the members of the Committee and most of the men in Germany prominent and influential in politics, finance and business, the so-called "keymen," about the bank plans, and upon general principles there is substantial agreement.

There has also been a great deal of discussion all the time about the matter of payments, outside of Germany, on reparations. It is assumed that in time there will be a substantial surplus of revenues to be applied to reparations. Every one believes it will be easy to use this surplus in making payments for reparations outside of Germany, to the extent that there is a surplus of exports over imports and nearly every one realizes that it will be difficult and dangerous, if not impossible, to make any payments beyond the limit of this surplus. But the credit piled up in the bank may be used to increase production and thus to make the surplus of exports over imports larger. It seems very simple to say that the surplus of governmental revenue must be deposited in the bank to the credit of the reparation account, and that this account shall be in charge of a commissioner, who would act under the direction of the Board in such a manner as to protect the bank and maintain the parity of foreign exchanges by refusing to draw upon the reparation account when the mark was a certain number of

points below par, or by accepting and honoring sight drafts at some times, and at others giving notice that he would accept only sixty or ninety day drafts. But there are many things to be considered, and there is reason to exercise the greatest caution because of the calamitous effect likely to be produced by a financial panic, or depreciation of the currency during the very period so carefully planned for Germany's reconstruction.

Mr. Kemmerer has written two discussions bearing upon this matter, and Mr. Davis has commented on them. Others have written and these men have written other comments on different aspects of this problem, but these are reproduced here both to show the form in which material is presented to these committeemen and to indicate just what factors must, among others, be considered when planning a method for making payments beyond the territorial limits of a nation.

18 rue de Tilsitt, Paris.
January 26, 1924.

Memorandum for Mr. Dawes.

Subject: Effect of Reparation Payments on Currency Stability

By E. W. Kemmerer.

A question frequently raised is whether substantial payments by Germany in the reparation account would seriously endanger a gold standard currency in Germany, if one should be established along proper lines. In the judgment of the undersigned, E. W. Kemmerer, J. S. Davis, Leonard P. Ayres

and W. S. Tower, there would be no serious danger to such a gold standard if the payments required should not be very excessive. Briefly stated, the fundamental reasoning underlying this opinion, is as follows:

Gold moves in international trade for the same reason and in response to the same fundamental motives as does any other commodity, *e. g.*, wheat, copper, steel, etc. It always tends to seek the best market and it moves in response to the profit-seeking motives, from the place where it is relatively cheap, to the place where it is relatively dear. It is cheap where the supply is large, relative to the demand—the chief factor in the demand being the monetary one—and it is dear where the supply is small relative to the demand. When gold is performing an important function in a given country which the public demands and for which it is willing to pay in goods and services, as, for example, the function of providing a stable currency through serving as money in reserves against bank-note issues or through actually circulating as money from hand to hand, a progressive reduction in the supply of gold, with a fairly constant demand, will make gold increasingly valuable at home as compared with other commodities (as well as decreasingly valuable in the markets to which it flows), and this increasing value at home and decreasing value abroad will, under normal conditions, tend to check its exportation.

A country that is a large producer of wheat and which exported wheat in substantial quantities, might increase its exports of wheat considerably in order to provide funds abroad for the payment of reparations, or for similar purposes, and to that end might reduce materially its normal consumption of wheat. The more wheat is exported, however, the scarcer wheat would become at home, and the higher its price would become, as compared with

other goods. If an increasing proportion of the home production should be exported for some time, the price of wheat at home would become so high that it would be cheaper for the country to export something else than wheat, in order to provide the necessary foreign credits. A country whose people liked wheat products and were willing to pay for them, clearly would not permit itself to be deprived of all its wheat in order to provide values abroad with which to make the necessary foreign payments. Those values would be provided by the exportation of a great number and variety of articles—all tending to be in such amounts and proportions as to represent the minimum total sacrifice at home. Given a reasonable length of time, prices of the different kinds of commodities would adjust themselves to this end.

The same principle applies in the case of gold, which differs from wheat, from the point of view of the present problem, chiefly in the fact that it is usually more highly marketable in the world's markets than wheat, and that the chief demand for it is the demand to meet the needs of a stable circulating medium instead of a goods need. These differences are of little importance from the standpoint of the present problem. If the country on the gold standard has a strongly unfavorable balance of payments, exchange rates rise to the gold export point and gold flows out. The more gold flows out, the dearer it becomes at home, this dearness being expressed in:

(1) Falling prices of those commodities and securities whose prices are sensitive;
(2) Rising interest rates, first on call and short loans, and later on loans of longer maturities.

A long continued outflow of gold usually results in an increasing uneasiness on the part of the banks

and the financial public because it appears to be excessive and to threaten the monetary standard.

Furthermore, high and rising exchange rates penalize the importer of goods and securities and benefit the exporter, because the importer is compelled to pay more for his exchange in terms of the home money, while the exporter receives more in terms of the home money for his foreign bills. Just the opposite situation, of course, develops in the country which is receiving the gold.

These forces become cumulative, and soon check the outflow of gold and cause payments abroad to be effected by the shipments of other commodities or securities which have become progressively cheaper in terms of gold; in other words, the commodities and securities whose prices have been falling under the pressure of heavy gold shipments. In the country receiving the gold, however, prices will have been rising and interest rates will have been tending downward under the influence of this influx of gold.

Of course a people, in time of great emergency, may decide that a gold standard is a great luxury which they can not afford, just as they may decide, as a matter of patriotism, to forego the use of wheat bread and eat only black bread. This, however, is not likely to be the case among a highly civilized people in time of peace. A country can always have gold if it is willing to pay for it.

The natural economic forces above mentioned, that come into play to protect a country from undue drain of gold, may be strengthened by legislation requiring:

(1) Definite legal gold reserves against notes and deposits with a progressive tax on deficiencies, the proceeds of which would go to the government;

(2) Publicity in regard to gold holdings of the banks (and of the government, if it issues notes), so that the public will be promptly informed what is happening.

Of course if a country would import, in goods, services, securities, etc., for a long period of time, more than it should export and should pay the differences in gold, it would obviously sooner or later be deprived of all of its gold, unless it should itself be a great producer of gold. But it is equally true that if it should import goods, services, securities and gold in excess of its exports, other than coal, and should pay for the differences entirely in coal, it might be deprived of all its coal.

The foregoing discussion should not be interpreted to mean that it may not be advisable to place some restrictions upon the rapidity with which the Reparation Commission may draw against the funds accumulated to its credit in the bank.

15 Bellevuestrasse, Berlin
February 4, 1924.

Subject: Some Notes on the Alleged Danger of a Breakdown of the German Gold Standard through Excessive Calls for Gold against the Reparation Credits which it is proposed to build up in the New Gold Bank in Berlin.

By E. W. Kemmerer

For the sake of illustration, assume that a billion gold marks have been accumulated on deposit account in the Bank in Germany to the credit of reparation account; assume that banks in France sell for the account of the Reparation Commission to French importers of goods from Germany, drafts on this deposit in Germany payable in gold marks

which drafts French importers send to German exporters in payment for the goods which they are importing from Germany. The German exporter deposits the draft or the proceeds thereof to his own credit, either in the new gold Bank or in some other German bank in which he keeps his account, with the result that:

(1) The German exporter now has the deposit credit that the Reparation Commission formerly had;

(2) The French importer has the goods which were exported from Germany for which he had made full payment;

(3) The Reparation Commission has received its money in France;

(4) The German Government has been credited with the corresponding amount on reparation account which it had previously placed in the new gold Bank in Germany out of the proceeds of taxes;

(5) The banks of Germany have lost no gold although a transfer of gold may have resulted from the new gold Bank to some other German bank in which the German exporter keeps his account.

If the Reparation Commission should sell an undue amount of these drafts to French importers and bankers, exchange rate in Paris on Berlin would fall to the gold import point for France and gold would move from Berlin to Paris. The counterpart of this movement would be a rise of exchange rates in Berlin on Paris to Berlin's gold export point and the shipment of gold from Berlin to Paris.

If this situation should continue long, automatic economic forces would come into play to check and ultimately to stop the undue exportation of gold from Germany to France. Among these forces would be the following:

(1) Falling prices in Germany and rising prices in France, which would make it increasingly prof-

itable for France to take her German credits in goods and securities rather than in gold and, conversely, for Germany to pay France in goods and securities rather than in gold;

(2) Rising interest and discount rates in Germany and falling interest and discount rates in France which would make it increasingly profitable for international bankers (including the French) to divert floating funds to Germany and away from France;

(3) Decreased returns for the Reparation Commission and decreased profits for French exporters on each thousand marks of German credits in Berlin against which they were drawing drafts because of the low and declining number of francs obtainable for each thousand gold marks at the reduced exchange rate prevailing in Paris on Berlin;

(4) Increased profits for French merchants importing merchandise, securities, etc., from Germany because of the lower prices they would need to pay for their Berlin drafts on account of the low exchange rates in Paris on Berlin;

(5) The forcing of the Paris-Berlin exchange rate out of equilibrium with the other international exchanges, with the resulting profit to bankers in London, New York, Rotterdam and other financial centers, in transferring funds to Berlin by arbitrage through Paris because gold mark credits could be bought through Paris more cheaply than by purchase of bills directly in Berlin. This would force Paris to pay Berlin for the account of London, New York, Rotterdam, etc., would force up exchange rates in Paris on Berlin and stop the flow of gold from Berlin to Paris;

(6) The French would find it increasingly profitable to remit to New York, London, Rotterdam, etc., by arbitrage through Berlin because of the low rates in Paris on Berlin, and because of the pre-

E. W. Kemmerer

sumably low exchange rates in Berlin on other cities, due to the scarcity of gold in Berlin, high interest rates, etc.

Gold moves in international trade under the influence of the same fundamental forces as does any other staple commodity. It goes from the place where it is relatively redundant, therefore relatively cheap, as compared with other goods, to the place where it is relatively scarce and therefore relatively dear; and it continues so to move so long as the difference in its value in the two countries is sufficient to pay shipping expenses and to yield a reasonable profit to the shipper. But every shipment of gold lessens the supply of gold in the exporting country, and thereby tends to make it dearer there in comparison with other goods. Every such shipment likewise increases the supply of gold in the importing country and thereby tends to make it cheaper there in comparison with other goods. These forces, both working in the same direction, soon check the outward flow of gold for the same reason that they would check an excessive exportation of wheat, or any other commodity, say from the United States to Germany.

If there is a fund in Germany to the credit of the Allies, payments from that fund, if unrestricted, will be made chiefly in commodities which Germany will herself produce to advantage in the field of international competition, or in commodities shipped from other countries to the Allies and paid for out of the proceeds of Germany's exports of her own staples to those other countries. The Allies will receive their pay, for example, in coal, dyestuffs, potash, and the like, directly from Germany, and also in coffee from Brazil, cotton from the United States, hides from Argentine, etc., for which Germany will have paid by the shipment of her own products to those countries. Under the play of in-

ternational economic forces, Germany would not make her payments in any one commodity—coal, dyestuffs, potash, *or gold*—because heavy payments in any one commodity would be uneconomic for Germany to make and likewise uneconomic for the Allies to receive. Payments would be made in a great number of commodities and the varying proportions of each in the total settlement would be adjusted through price movements in Germany and abroad, so that the goods exported from Germany in connection with reparation payments would probably be much the same in character and in percentage distribution as the goods exported from Germany on her general trade account.

If the Allies should take too much of Germany's total economic product, they would obviously impoverish Germany and in doing so reduce the health and efficiency of Germany's population, and thereby force a reduction in Germany's productivity through causing (1) an increasing emigration of German labor, (2) an increasing death rate, (3) a decreasing birth rate, and (4) a decreased productive efficiency on the part of the German population remaining at home.

In making the above statement, it is not intended to take the position that no restriction whatever should be placed upon the withdrawing of the funds accumulated in the new gold Bank to the credit of reparation account. The mere fact that the placing of reasonable restrictions might inspire greater confidence in the Bank among those not familiar with the strength of the above mentioned automatic economic forces might itself be sufficient reason to justify some restrictions. It might, for example, be provided that drafts on the account drawn by the Allies or their representatives should be wholly or in large part time drafts, instead of cables or demand drafts; furthermore, that such drafts might

always be paid by the new Bank in its own notes or in deposit credits, so long as the mark were maintained on a gold basis, and that the Bank might have the option of redeeming its notes in gold drafts on New York or some other financial center on the gold standard, in accordance with the principles of the gold exchange standard. In this connection, it should be understood that the price charged for such drafts in Berlin should never be above the gold export rate. Other possible restrictions will be mentioned in a subsequent memorandum.

In the above discussion it is assumed that the new Bank will be required by law to maintain a reasonable gold reserve—probably thirty to forty per cent. in its own vaults for on deposit abroad—a reserve adequate to take care of normal seasonal swings in the demands for currency and in addition to provide a reasonable factor of safety for emergencies. It is also assumed that, in accordance with the suggestion I made in a previous memorandum, the deficiencies in this reserve will be subjected to a progressive tax somewhat similar to the one provided for in the United States Federal Reserve Bank Law.

15 Bellevuestrasse, Berlin.
February 5, 1924.

Subject: Mr. Kemmerer's Memorandum of February 4, 1924, entitled "Some Notes on the Alleged Danger of the Breakdown of the German Gold Standard."

By J. S. Davis

This memorandum deals with a subject on which I have been working for some days and on which I have a memorandum in preparation. The point is

one of large importance on which it will be unfortunate to have conclusions crystallize prematurely. Such discussions as we have thus far had have shown some differences of opinion which are likely to be reconciled before long. In the meanwhile, however, I wish to record my inability, in spite of my agreement with much of Mr. Kemmerer's memorandum, to accept his conclusion, as stated, that, "If this situation should continue long, automatic economic forces would come into play to check and ultimately to stop the undue exportation of gold from Germany to France." That these forces would operate *in the direction* Mr. Kemmerer points out, is clear; that they would operate *to the extent* of stopping the undue exportation of gold, without the interposition of additional important restrictions upon withdrawal (beyond those mentioned in his last paragraph) is, in my opinion, by no means certain. This will depend, among other things, upon the size of the deposit in relation to the possible increase of Germany's excess of exports (of goods and services) over her imports (of goods and services); and also upon the extent to which gold or gold balances moved out of Germany affect foreign prices and money markets. Given time, no limit can be set to Germany's export surplus, but it is incapable of rapid expansion in a brief period, at least from the point at which it stands when fairly normal economic conditions are regained; and the extent to which gold movements will influence prices, under post-war conditions, can not be predicted with confidence.

I believe there is a limit, not readily ascertainable in advance, up to which withdrawals of such deposits will in no way endanger the stability of Germany's currency, banking and exchange, but beyond which such withdrawals would, even under such restrictions as suggested in Mr. Kemmerer's last

paragraph, jeopardize this stability, and if continued, destroy it. Against exceeding this limit, I believe that provision for safeguards must be carefully made.

Paris, February 17, 1924.

On Wednesday, before leaving Berlin, General Dawes called upon Chancellor Marx to express the appreciation of the Committee of the cooperation of the German Government, and Herr Marx told him privately that he felt that in the action of this Committee, there existed the last hope of a reasonable economic settlement. Ambassador Houghton was quite hopeful toward the latter part of the Committee's stay in Berlin, and no man knows better the difficulties of the problem than he does.

CHAPTER V

FORMULATION OF REPORT—ATTITUDE OF FRENCH PRESS TOWARD WORK OF THE COMMITTEE—FALSE RUMOR OF RESIGNATION OF GENERAL DAWES AND EFFECT ON FOREIGN EXCHANGE—COMMENTS AND MEMORANDA BY AMERICAN EXPERTS ON ACCUMULATION OF BUDGET SURPLUS WITHIN GERMANY—DISCUSSION OF WITHDRAWAL OF ACCUMULATIONS ON REPARATIONS PAYMENTS—PROSPECTUS OF GOLD BANK TO BE FORMED BY DOCTOR SCHACHT—ANNOUNCEMENT BY COMMITTEE OF PLANS FOR ESTABLISHING NEW GERMAN BANK OF ISSUE.

Paris, February 17, 1924.

On the train returning to Paris General Dawes talked quite confidentially of his conception of the plan which ought to be formed and of the progress already made, and at the risk of repetition it is stated in his own words.

"The principles upon which the report must be based, at this time, define themselves roughly in my mind as follows:

"1. The whole report should be constructed upon the fundamental principle that the people of Germany must bear a burden of taxation for debt-paying purposes, equal to that borne by the Allied Nations. This principle is easy to state, but presents great difficulties when it comes to expressing it in figures under present conditions.

"2. It is presupposed that the plan is an elastic one, and that the burden of taxes upon Germany increases in prosperous years and lessens in years of depression, automatically. In this connection, in my judgment, it will be necessary, within limits, to invoke the Kemmerer idea of fixing as a basis for payments, a percentage of gross government income.

"3. The plan, in its broader aspects, must be so drawn as to impress on the public mind that it assumes, in its eventual functioning, normal economic conditions in Germany under a stabilized currency and a balanced budget. Waiving, for the moment, the question of an exportable surplus, the amount which Germany might be expected to pay in taxes, under recognition of the principle of a commensurate burden with that of the Allies, will perhaps then resolve itself into at least a reasonably definite figure. Since the plan is elastic, however, and so drawn that income will increase with Germany's prosperity, care should be had not to let the minimum figure guess destroy perspective. The plan must not assume, that, with a prosperous Germany, the figure will not be commensurate to those obtaining in other countries. Ground exists for optimism in viewing the future of Germany under favorable economic conditions. If an estimated minimum is in the minds of the experts, they must remember that all these things are matters of estimate, and that the business instinct of the world assumes that with a restored Germany, all ordinary limits will be exceeded. If the report is so drawn

as to run counter to this instinct, which is probably right because it is an instinct, the report will fail and the efforts of the committee fall to the ground. The experts should remember that the leveling of the economic barriers in the Ruhr is one of the objects sought to be accomplished by this effort, and not the promulgation, through the world, of well guarded opinions upon matters admittedly of estimate only.

"The creation of a bank of issue, operated under allied supervision, as provided for in the bank plan proposed by the committee, with the provision for the deposit in the bank toward reparations of the internal surplus arising from the scale of taxation proposed roughly commensurate with that borne by the Allies, makes possible the promulgation of the idea of commensurate German taxation.

"4. Since the creation of the balance in the bank for reparations account by the deposit of the internal taxation surplus, becomes the basis of any payments, including deliveries in kind, which the existence of any exportable surplus, or the transfer of securities representing capital values renders possible, the practicability of the creation of the deposit without adverse effects upon Germany's internal business, must be explained. In this connection, it will be remembered that the German savings-bank deposits before the war were about twenty billions of gold marks, indicating the large amount of capital required by Germany in a normal year's production and evidencing the large sum which can be accumulated internally before a con-

dition of normalcy is reached in German productivity, and it should be remembered that a large balance of purchasing power in the hands of the Allies, which can be spent only in Germany, will have an effect in increasing the demand for German goods, both necessities and luxuries. A portion only of this balance can be transferred externally through exchange and transfer of capital values and the rest of it can not be spent anywhere else than in Germany. It must be assumed, however, that the Allies will not commit industrial suicide by allowing this money to be used for the transfer of German goods to such an extent as to cripple their own industry. It is evident that difficulties are involved in this question, which require careful consideration.

"5. Since all agree that the return of German productivity depends upon the economic reuniting of the Ruhr with unoccupied Germany, we must plan to provide for certain immediate definite guarantees to France, commensurate with the value of the incomes which she is giving up in the Ruhr, including deliveries in kind. This is one of the most important features of the plan, involving discussion of the possibility of immediately making the German railway system the basis of creating revenue bearing securities to be used in this connection. Probably other gages must be given. General supervision of the Ruhr, as distinguished from economic control, must be conceded to France, not only in the interest of her proper protection, but as safeguarding the performance of the entire program in the future.

"6. If resort is had to the creation of monopolies, under allied control, in certain resources of income, such as those of tobacco, alcohol, etc., in either furnishing gages to France or as guarantees for reparation payments direct into the bank, it is most desirable to have them limited and to have the possibility of profit therefrom to the managing agency, the smallest consistent with the proper exploitation of the revenue. With the world prejudice existing against monopolies, intensified by the feeling regarding the German industrialists, the plan must not, even in appearance, turn over the German people to private exploitation. As a principle, it is wise to have the Allies deal with the German people through their government and not assume direct relations with them in the matter of the imposition of collection of taxation. To obtain the minimum of guarantees sufficient to effect the general economic liberation of German business, it may be necessary to resort to monopolies. I hope not, yet if so, it is suggested that the German Government, with allied supervision, be the agency used, as far as possible, in their creation and functioning.

"7. The plan must suggest a moratorium of reparation payments, with the exception of certain necessary minimums like that necessary for an appropriate force of occupation.

"8. Depending upon the conclusions of the Committee as to the present balancing of the budget, the question of the amount and means of securing a foreign loan for the balancing of the budget should be covered. In regard to the bank, it is assumed

that the rate of earnings which the plan makes possible upon the stock of the bank will contribute a sufficient inducement for the transfer of such portion of its capital as is required from the allied countries.

"9. The plan must be so drawn, in relation to public opinion, as not only in its functioning to provide German business the necessary incentive for recuperation, but to convince public opinion that it is so constructed. On the other hand, it must give the Allies the reasonable assurance of adequate reparations."

This statement having been typed, Colonel Logan showed it to Monsieur Barthou and made an engagement for General Dawes to have a conference with the latter Saturday afternoon. At this conference there was a full discussion with Monsieur Barthou of the general outline of the plan.

Mr. Young, Mr. Crocker and Mr. Tileston did not return with us to Paris, but went to Nuremberg and reached here on Sunday in time for the next meeting of the Committee, which is on Monday, the eighteenth, at eleven o'clock.

Now that the Committee is really "coming to grips" with their problem, it does seem that the hope of accomplishment is better than ever. It was partly the context and partly the manner of reporting the chairman's speech that created about this conference, in the public mind, an atmosphere of frankness and freedom from diplomatic ceremony. Such expressions as "foul and carrion loving vultures, the nationalistic demagogues of all countries"

and "impenetrable fog banks of economic opinion" attracted wide attention and favorable comment as indicating, what is actually the case, that this Committee could work without the restrictions imposed by personal political ambition and interest. The emphasis placed upon "the great disaster which faces each Ally and Europe unless common sense is crowned king" really had a sobering effect upon the politicians of European countries at least, and especially as it was connected with the warning that just as the war might have been lost through the lack of unity of command so the prospect of a settlement is now jeopardized by the present lack of unity. These expressions, which have been characterized as plain speaking, have drawn to the attention of all public men the really grave disasters which threaten all Europe. They all realize that the world is sick and tired of this unsettlement and alive to the danger of a catastrophe which may befall unless some constructive action be taken promptly. The action of the Committee in calling in Doctor Schacht was taken as an indication of its independence and courage. French papers were surprised that there was no delay and no effort to explain to the French public why the plans of a German should be so carefully studied, but they approved of this action. It appeared abrupt and undiplomatic but businesslike and practical, and, sobered by threatened disaster, they have withheld all criticism. Then the trip to Germany was likewise approved both here and in Germany and very greatly improved the chances for the complete coopera-

JAMES A. LOGAN
Unofficial Observer for United States at Reparation Commission

tion of the German Government in the effort to make a settlement.

The conditions that now exist in Germany seem favorable to the gaining of support for any practicable plan that can be offered quickly. Germany is demoralized but not too far gone to be saved by prompt action. Her currency is for the moment stabilized, taxes are being paid on the basis of gold marks, the government pay-roll is being cut down, and its revenues are rapidly overtaking its expenditures. Doctor Schacht's plan has the unanimous support of the German Government and leading men of business. The adoption of this plan and the universal acceptance in Germany of the justice of bearing an equal burden of taxation seem to give promise of cooperation from that country without creating a corresponding opposition in other countries. There really appears to be the prospect of more unity between the Allies and of better understanding with Germany.

Doctor Stresemann, the German Foreign Minister and former Dictator, was quoted in the papers of to-day as having said in a public speech at Elberfield: "When I reflect on the negotiations conducted in Paris and Berlin by the Committees of Experts, for the first time I see the glimmer of dawn on the horizon."

Tuesday, February 19, 1924.

The morning *Herald* contained to-day quite a long article from which are taken the following hopeful sentences. As a matter of political gossip,

it was stated that Poincaré had called a conference of the French members of the Reparation Commission and of the Committee of Experts and several of his own ministers to discuss in detail the progress being made by the Committee toward a decision. They probably had before them this draft which General Dawes handed to Barthou:

"As a result of their conversations in Berlin, the members of the two Committees have returned here more optimistic than ever on the possibility of arriving at a unanimous report that will serve as the basis for an entire European readjustment. Not only did the Germans meet the experts with candor and open their books to them, but they appeared to be willing for the first time, virtually to commit the financial future of Germany to these business men. . . . From present indications, the experts favor recommending the return of the economic control of the Ruhr to Germany, the details of their plan demonstrating that the net result of this will mean more to France than if she insists on retaining her present control of Ruhr industries. Militarily and politically but not economically France might still retain control of the Ruhr. The maintenance of economic barriers will be disapproved as well as the present disseverance of the German railway system. In return France would get the promise of regular reparation payments, virtually guaranteed by the new factor the Committee would introduce of an international issuing bank absolutely controlling German currency and furnishing the basis of the new situation. This bank has been regarded from the start as the key to the problem which the experts had to solve."

February 21, 1924.

Another comment from a New York paper which has just been delivered may be found interesting. It was about February eighth in Berlin that we were called at midnight to the telephone and, General Dawes not being available, it fell to my lot to deny strenuously a report said to be circulating in Amsterdam and New York to the effect that he had resigned from the Committee. Doctor Schacht had just made a speech which was interpreted in some quarters as indicating friction between him and the Committee. We realized this was a gambler's rumor circulated for its effect on the stock exchange. The Rentenmark and the paper mark are stabilized in Germany for all practical purposes at a value for the paper mark of four trillion, two hundred billion to the dollar, and for the gold mark and Rentenmark of four and two-tenths to the dollar, but upon the exchanges there has been constant trading at figures varying somewhat from these. The New York paper printed the following article:

"The German paper mark, which for nearly two months had been the steadiest as well as the cheapest of all currency listed on the foreign exchange market, suffered another dizzy sinking spell yesterday. The break attracted international interest, for it occurred not only in New York, but also in London, Paris and Berlin and other countries. Explanations were hard to find and those advanced were based only upon unconfirmed rumors. From December eleventh to Thursday the paper mark had maintained a steady value here, the figure of 4,348,000,000,000 to the dollar having been un-

changed. In yesterday's dealings it was quoted at an even 5,000,000,000,000 to the dollar. Even though any quotation is purely nominal the slump attracted attention; in fact, foreign exchange dealers said the absence of any commercial dealings involving the use of the paper mark made the break even more puzzling.

"In London the paper marks suffered an equally sharp reduction. Up to yesterday the quotation had been given as 18,000,000,000,000 marks to the pound sterling; yesterday the quotation was 21,500,000,000,000. This shrinkage amounted to a shade more than 13 per cent. The shrinkage in New York was an even 13 per cent.

"But the intangible factor in the situation and the one to which the break was attributed primarily, was the rumor that General Dawes had abandoned suddenly his work on the sub-committee of the Reparation Commission. This rumor was current virtually in every active foreign exchange house in the financial district; cables from abroad had carried the rumor, and, once here, it was relayed from house to house as a result of the efforts of dealers to 'run it down' and learn for themselves whether or not it was true. Neither a denial nor a confirmation was obtained during the full day of trading. The nearest approach to a denial that could be found was the information that news service from Paris had up to that time carried no message on the subject.

"The rumored resignation of General Dawes was attributed to several alleged grievances, one supposedly being indignation over the Washington incident and another on the supposition that all was not well in the work of his special committee. Food for the Dawes rumor was found in the fact that other principal foreign exchange rates were lower. The French franc gave way both in New York and

in London. The New York quotation was 4.52½ cents as low and 4.53 cents closing. This represented a decline in a day of 12 to 12½ points or one-sixth of a cent. Belgian francs were off 10½ points, while the Italian lira gave way 1¼ points. The English pound sterling was quoted at $4.29⅝, as against the previous closing price of $4.32⅛. This represented a decline of 2½ cents in a day, which was considered unusually sharp."

Again on Tuesday, February nineteenth, here in Paris, I was called at midnight by a newspaper editor who stated that other papers here had the story of an interview with Mr. Young to the effect that Poincaré was obstructing the work of the Committee and that in consequence the American members of the Committee intended to resign. Possibly a prompt denial resulted in this rumor not being printed. We did not see it, but the franc was selling at its lowest point at just that time, and if such a report had gained credence, it would not have tended to strengthen it.

The discussions arising out of the memorandum submitted by General Dawes on February eighteenth have only emphasized the importance and the delicacy of the French position in the Ruhr. This decisive act of invasion, defended and supported by the French nation, has been criticized by many English and American writers. It has become a bone of political contention in England and the subject of much discussion in America. Whatever may be the legal aspects of the case, and outside of France and Belgium the preponderant opinion seems to be adverse to the French claims, there is no doubt that

public opinion in France supports the position of the French Government. The acrimonious discussion has aroused the national pride of France and the Frenchmen believe not only that their action was right, legal and necessary, but that it was essential to their safety and the protection of the nation's interest. Those in control of the government, whatever their personal opinions may be, must respect this public opinion. The necessity under which the Committee is working, of coming to some unanimous agreement, makes it unnecessary or even impossible for them to discuss the propriety, legality or necessity of the Ruhr invasion. They must take the situation as they find it, and make such recommendations as can be supported by the French and Belgian members of the Committee. General Dawes, however, on February twenty-second submitted to Monsieur Barthou the following memorandum designed to remind those who are responsible for France's position of the importance of creating throughout all the world the impression that the basis is being laid for a lasting peace, and thus for providing the conditions under which an extension of credit would be made from those parts of the world where it is redundant to the nations which are so urgently in need of it.

"18 rue de Tilsitt,
"Paris, France.
"February 22, 1924.

"The following observations suggest themselves as bearing upon the problems in connection with the

Ruhr situation, the solution of which will be determined chiefly by the attitude of France.

"(1) It is presumably desired by all, including France, that in any new status quo established by the acceptance of the experts' plan, the normal economic functioning of Germany shall not be embarrassed.

"(2) Based upon the discouraging experiences of France and all the Allies with the German spirit of cooperation, in the past, France, with justification, will probably urge that her full release of economic pressure in the Ruhr must not be complete until the plan is accepted, not only by the Allies, but by Germany. When the plan is accepted by all, including Germany, and an allied loan made to Germany, either by the allied governments or the citizens of those governments, including, it is hoped, citizens of the United States, it is in practical effect, a new treaty of economic peace between an allied entente on the one side and Germany on the other. If, in the mind of the world, it falls short of this conception, the contribution of foreign capital necessary to its establishment would be probably greatly hindered.

"(3) It must be evident that the mere creation of this new status quo of economic peace involves a protection for France greater than that which can come from an economic pressure in the Ruhr, which can evidently result only in the complete economic break-down of Germany, and the loss of any hope for adequate reparations, thus dangerously jeopardizing the present and future interests of France.

"(4) The great importance, therefore, of the determination by France of her proper attitude in this situation, is readily apparent. In my judgment, it was only her courage to act in moving into the Ruhr which has precipitated the conditions and emergencies which have rendered possible an economic peace which is really to be an economic peace. Had it not been for that action, this Committee would not be in existence.

"It is again that splendid courage of France, in decision and action, in terms of the withdrawal of economic pressure, upon which the new economic peace must depend.

"(5) I fully realize how unimportant are the opinions, as to what France should do, of outsiders, who can not properly sense the minds, consciences and instincts of the great mass of her people, as do those who are charged in this crisis with the great responsibility of determining her action. As one of the elements, however, which enters into their considerations of a wise decision, the reaction of an American upon certain things may possibly be useful.

"Nothing is more timid than capital. It is essential to the operation of the plan that the decision of France, as to the course which she is to pursue in lifting the economic pressure as distinguished from such military supervision in the Ruhr as will give her protection, shall be such that foreign capital may not be frightened from participation. Indeed, the participation of foreign capital, in carrying out the plan, may well be regarded by France as the

final evidence that at last a solution has been reached which is durable, and which has behind it a common allied interest in its continuance, thereby affording the best safeguard for the future of France.

"If France insists upon methods, in lifting the economic pressure in the Ruhr, which creates the impression upon the foreign investor that the new status quo may be disturbed or changed by quick or unconsidered decision, individual foreign capital is not likely to participate. This would indicate that the best possible plan for all concerned has not been followed. The part of wisdom, therefore, would indicate that when the present economic pressure is lifted there shall be reasonable assurances that it will not be reimposed, except for self-evidently sufficient reason and by concerted action.

"On the other hand, if foreign capital is to participate, it should be assured that its contribution will not be asked until France and the Allies are satisfied as to the sincere spirit of the promised cooperation of Germany, and that the plan is in such shape as to be launched in its entirety. The maintenance of some degree of economic pressure, therefore, pending the completion of the plan, would seem justifiable, not only to bring about its speedier consummation, but to assure all that, when this pressure is lifted and the plans once entered upon, it will be continuous in its operation.

"The American individual investor, as distinguished from the European Allied Governments, will look upon the plan chiefly from the standpoint

of safe investment. He is not influenced, as a European Ally might be in considering an advance of money through governmental banks, by any direct thought of the effect of the advance upon reparation payments. His probable attitude, therefore, toward a prospective loan to Germany, and the conditions under which it is issued, may be regarded as good outside evidence as to what it is desirable for France to decide in connection with the method of dealing with the Ruhr situation.

"It is to be hoped, in the interest of the plan, that consistent with her full protection, France will be able to suggest methods which will impress the individual foreign investor with the safety of participation in the loan to Germany."

In this connection it may be interesting to refer to an article sent by request over the telegraph wires by General Dawes to *The Literary Digest* and published by that magazine in its issue of January 27, 1923:

"The resumption of the orderly progress of civilization in Europe and the world depends upon a reasonable settlement of the reparations question under which, while proper reparations charges are met, the incentive to effort on the part of the German people is not destroyed. Nobody differs on this point, but nearly everybody, for four years, differed on how to bring it about. Public sentiment all over the world at the end of the war was like molten lava from a volcano, it was uncontrollable and not plastic. It has not yet had time to cool off everywhere. The position of the United States at the Versailles

conference was for reasonable reparations, but public sentiment in England and France at that time made agreement impossible. The power of international negotiators since the war has always been limited by public sentiment at home. Whenever a negotiator stood for common sense in advance of domestic public sentiment he was either compelled to change front as Lloyd George did, or leave office as did Briand. As time has gone on, public sentiment in England and the United States has cooled down, so that common sense on the part of the masses is again reasserting itself, irrespective of nationalistic demagogues. The elemental changes in public sentiment, however, are determined by events and not by leaders. Germany, in the economic war following the Great War, has dealt with a coalition in disagreement between themselves, and this selfish disagreement among the Allies, together with the results of the planned degradation of the mark, has created a feeling among the German people that it is possible to avoid payment of proper reparations. No German government, strong enough to enforce collection of the taxes involved by proper reparations, has been possible in Germany up to this time because this feeling existed. On the other hand, public sentiment in France, which suffered the most by the war, could not be solidified behind a government strong enough to put through a proposition for reasonable reparations. To the protest of the German government against the invasion of armed troops into a peaceful population the French national conscience answers 'Belgium.'

"The invasion of the Ruhr by France, therefore, is in my judgment essential, both to bring France to a realization that only reasonable reparations can be collected and to bring Germany to the knowledge that it can not avoid its payment. It should be remembered that the great French army to-day is the

safeguard of civilization in Western Europe. No one need fear Bolshevism at this time in Germany, pending the inevitable ultimate decision of the German people to form such a firm government that it can take the economic measures which will get them rid of the French Army, just as France did when the German Army in 1871 occupied Paris. At the same time demonstration of the impossibility of the collection by armed forces of reparations directly from the German population, the underlying business common sense of France, which needs money, the fact that she now is dominating the situation and will not have a compromise forced on her by others, will bring French sentiment the more speedily to the reasonable view. Stinnes, the leading business man of Germany, in a recent address before the German Economic Council, and Louis Locheur, the leading business man of France, in an address before the Chamber of Deputies, have each outlined in terms of reason the solution of the reparations question. As Stinnes says, the mark can not be permanently stabilized by an international credit. Germany can stabilize the mark and pay its reparations only by an exportable surplus of material, and can only create that surplus by a ten hour day's work instead of an eight-hour day.

"Locheur's speech is practically to the same effect. The last event in my judgment necessary to bring France and Germany to a common sense reparations settlement was the invasion of the Ruhr district by France. I realize fully that what I have said is not the present view generally of the press of the United States or of our people. I have not discussed the matter from the standpoint of right or wrong. This immediate situation is not one in which long distance academic discussions will have much effect upon European realities. The last four years show that in international matters events de-

termine policies rather than that policies determine events. Two things are especially desirable in the United States—less demagoguery in Senate debates, where the pleasing of uninformed local constituencies is an element in discussion, and more trust in the strength and wisdom of President Harding, who firmly, and taking one step at a time, is moving in the right direction. In my judgment the United States must face with courage instead of cowardice its unavoidable responsibilities, and I do not believe the policy of scuttle can with safety be ridden much longer by the demagogue. Moral principle, the dictates of humanity, as well as economic self-interest, all combined, will force the United States, with unimpaired sovereignty maintained, into that field of international duty which since the war it has not fully entered. In my judgment, irrespective of the present condemnation by the American press of the French move, it will be universally recognized and acknowledged long within two years of this time that the reasonable settlement of the reparations problems, which by that time should have been reached, was made possible by the situation precipitated by the French invasion of the Ruhr."

On the day after this statement of February 22, 1924, was submitted, Monsieur Poincaré was reported as stating to the Chamber of Deputies that one of the members of the Experts Committee had said, "If France were not in the Ruhr, we would not be here." And although the memorandum was not intended for publication, General Dawes, in an interview, confirmed the assertion, and was widely quoted to this effect. It certainly did no harm in France.

The effect upon the bank and upon the exchange

value of the mark, of excessive calls for payment in foreign exchanges of reparation credits, has already been discussed. An allied question of importance is the effect upon the bank and upon the business of Germany, of leaving large credits to reparation account in the bank. Sir Josiah Stamp had written a discussion of this question, note number four, and Mr. Joseph S. Davis of our staff has submitted a comment upon it. His comments seem to cover the whole subject so thoroughly and his views to be so nearly in accord with those of Mr. Stamp that to include only Mr. Davis' discussion will be sufficient.

Confidential.

Reflections on Sir Josiah Stamp's Note No. 4

Joseph S. Davis

"1. Note No. 4 deals with the effects of the accumulation of budget surplus within Germany, and reaches the provisional conclusions:

"A. That the raising of a large budget for the progressive internal use, as is done in Great Britain, is not *identical* in economic effect with the raising of a similar budget, a large part of which the community is not entitled to handle.

"B. That the latter course, carried to an extreme, would bring some rather extraordinary economic consequences in its train.

"2. These conclusions are expressed in much

Sir Robert M. Kindersley
English Member First Committee of Experts

more conservative terms than the discussion leading up to them. As qualified, I believe they are sound, but I believe the discussion magnifies the dangers to be anticipated and that, in their *context*, the conclusions are much stronger than can be supported. With all due deference to Sir Josiah Stamp, I wish, therefore, to suggest some criticism of his discussion and some considerations which tend to modify the effect of his note.

"A. CRITICISMS

"3. I agree that there is a real danger of taking from the German public for the benefit of reparation creditors an excessive sum, either in budget surpluses or in guaranteed revenues, and that this danger is not removed by limiting the amount of withdrawal of this sum to the amount of Germany's exportable surplus. But I believe this danger lies in the possibility of reducing to an intolerably low level the consumption of the German public and that it is mitigated rather than intensified by the investment of withdrawable balances in Germany's internal development. The consequences of attempts to collect too much will be seen in the early stages, in abnormal death rates, emigration, and so on, rather than only after a prolonged experience with the system.

"4. Taxation, *ipso facto,* reduces the incomes at the disposal of the taxpayers, but not necessarily his personal consumption, as is suggested in paragraph 2 of the note. At several points the note exaggerates, in my opinion, the extent to which Ger-

man consumption would be reduced by a burden of taxes that the government could collect.

"5. High taxation for an alien owner will reduce the effective standard of living only to the extent that it reduces consumption, not to the full extent of the taxes so collected, for much of these will come out of the taxpayer's ordinary savings. Moreover, by no means all reductions in standards of living are injurious to a people. The taxation may conceivably be so high and so ill-arranged as to make the maintenance of health and efficiency impossible for large sections of the population, and to drive them to emigration in large numbers to escape such intolerable conditions. But many economies in consumption are possible in an advanced nation, even in the so-called necessaries of life, without leading to such extreme conditions. The note appears to underrate the magnitude of such economies and the margin afforded by the ordinary savings of a productive nation. Even in periods of severe depression and under highly abnormal conditions, such margins are considerable, as have been illustrated in England and France in the past three years.

"6. Capital expenditures, met out of taxation, within the country, tend to be beneficial to the country if expended upon production goods, whether by the government or by alien powers, at least to the extent that the increased production resulting from their creation exceeds the interest charge on the funds so applied though it must be admitted that part of this benefit may accrue to reparation creditors later through increased exportable surpluses.

"7. The assumption that heavy investment in Germany, on allied account, will not benefit the German people, overlooks two important points: (1) that the effect of such investment is to lower production costs for domestic goods as well as the export goods, and so to increase the quantity of goods at the command of consumers with given incomes; and (2) to make for more continuous operations of Germany's economic organization, well provided with investment funds. The gain from the latter source is of a special importance. The distribution of productive effort between production goods and consumption goods, between goods for export and goods for domestic use, will continue to be made according to economic forces, which, through the medium of prices and interest rates, will ensure against serious gluts of consumption goods and the calamity of production falling 'still-born,' to which the note makes reference. Misjudgments will still occur, but such misjudgments, rather than the process as a whole, will be responsible for such temporary gluts as may be expected.

"8. The implication that the surplus that is being stored up in Germany must ultimately be withdrawn is, in my view, unsound. There is no likelihood that the investment as a whole will ever be liquidated. The claims against it, first held by Germany's reparation creditors, may be expected eventually to be widely distributed. Individuals will indeed shift their investments, or liquidate them, with loss or gain. The claims upon Germany's increased productive capital may ultimately be owned less and

less in the present reparation creditor nations, as investors elsewhere become ready to absorb them. But this process, if it occurs, is likely to be gradual and according to the play of well understood economic forces. It need not involve any large scale attempt at liquidation, much less the withdrawal of the capital goods themselves.

"B. SUPPLEMENTARY CONSIDERATIONS

"9. These disjointed criticisms can perhaps be better appreciated in the light of another discussion of the problem which in part overlaps and in part goes beyond Sir Josiah Stamp's note and the foregoing criticisms.

"10. In the first place, it must be emphasized that in modern civilized nations a large portion of current production is not devoted to producing goods for current consumption. Much less than the total production effort suffices for this. The balance—large in periods of business activity, small in periods of depression—goes to increase the sum of durable consumption goods, durable production goods and auxiliary stocks of circulating capital. The individual contents himself with a smaller amount of current consumption goods than the income at his disposal would enable him to purchase; the balance of his income, apart from gifts, etc., he saves; part of his savings he applies to the purchase of durable consumption goods, and the rest he invests in domestic and foreign securities.

"11. The effect of this, from a national standpoint, is a steadily increasing supply of durable con-

sumption goods and production goods at home, and in some measure abroad, in which individual savers have rights of interest. And when the government taxes its people for more than the cost of its current services, it ordinarily invests the surplus collectively in durable consumption goods and production goods and has rights of interest in these goods.

"12. Now the first effect of the plan to require Germany to raise by taxation a surplus of revenue, which it places at the disposal of the reparation creditors, is to reduce the income at the disposal of taxpayers. This may reduce their current consumption in some measure; if so, it will affect their consumption by trenching upon these elements which are considered most dispensable, and even the so-called necessities of life consist in no small degree of such elements. It will, however, cut more heavily into expenditures for durable consumption goods, and still more heavily into their individual and corporate savings. If taxation is properly arranged, and is not impossibly heavy in the aggregate, it will not reduce the health and efficiency of the people, but will largely place at the disposal of the government part of the savings the taxpayers would otherwise accumulate, and some additional savings which would not have been made except under pressure. Part of these savings the government, in turn, puts at the disposal of reparation creditors within Germany.

"13. Though measured in money terms, these savings will consist fundamentally of a complex of goods, for current consumption, for consumption as

durable goods, and for productive equipment; some of them will be used in Germany and some in various countries abroad. The process of consumption, saving and investment will be very much the same as if no reparation arrangement was made, but there will be three differences in effect: (a) the aggregate savings may be somewhat increased at some cost to German consumption; (b) consumption in the reparation creditor nations may be slightly increased; and, most particularly, (c) the rights of interest in the aggregate German savings which are not diverted to immediate consumption will be vested to a larger extent in the reparation creditor nations, or their nationals, and to a smaller extent in the German Government or German nationals.

"14. Just in what proportion these savings, placed at the disposal of reparation creditors, will be received—how much in consumption goods from Germany or elsewhere, how much in production goods in Germany and in other nations,—this will be determined by the relative demand for consumer's goods and producer's goods, upon the competition of different countries for these goods, under much the same conditions as always affect the balance between production for the present and production for the future. This balance will be adjusted naturally and gradually, if free play is given to economic forces. Suffice it to say that to a large extent reparation creditors will receive no goods, either direct from Germany or from other countries to which Germany ships goods, but interests in German and foreign capital investments.

"15. The further consequences must not be overlooked:

"(1) Increases in Germany's ability to produce economically, in consequence of increased investment in Germany, will increase her power to export, which tends directly to reduce the disparity between the annual reparation charge and the exportable surplus through which it can be currently withdrawn. This process alone might solve the problem under discussion.

"(2) Germany's international credit will be enhanced by her increased economic strength and exporting power, with the result that private investment funds will tend to flow to Germany, thus supplementing her balance of payments on current accounts in such a way as to increase the opportunity of Germany's reparations creditors, as such, to withdraw reparation balances. This will be offset in some measure by the flow of German private capital abroad, especially in connection with enterprises related to Germany's exports.

"16. The danger of heaping up surpluses invested in Germany to the account of reparation creditors, increasing at compound interest, is smaller if one realizes the existence of a certain automatic check. The heavier the pressure of such investment funds upon the German market, the lower will be the rate of interest upon them, and the slower the rate of increase. This same tendency to abundance of investment funds, if it appears, will operate to alter in favor of wage earners, the proportion of production going to wages as compared with in-

terest, and so to increase the real income of wage earners.

"17. If this reasoning is correct, it is inaccurate to say (as some writers have said) that Germany can really pay reparation only to the extent that the reparation creditors will increase their absorption of goods in consequence of the reparation settlement. Beyond certain limits, their peoples do not wish, in fact, to increase their consumption. Most of them would, in any event, increase their foreign investments in the next generation. In the long run, they will be found to prefer settlement largely in this other form. Unquestionably much larger sums in settlement of reparations can be absorbed in the form of interests in productive enterprises in Germany and scattered all over the world, which will be built up as a result of German productive effort in excess of the requirements of German population. Obligations between individuals are not settled by forcing the creditor to take additional goods, but in large degree by giving him *interests* that he regards as valuable. In the long run, Germany's reparation obligation, principal and interest, will be settled, so far as it is settled, to a large extent in the same fashion. If such form of payment is possible for Germany and acceptable to her creditors, who shall say that it can not effect a genuine payment?

"18. In short, it is not unreasonable to expect that, if peace can be maintained, the reparation debt of Germany will eventually be converted, in large measure, into holdings of securities by nationals of

reparation creditor countries based upon productive wealth (a) in Germany; (b) in the creditor countries, themselves, and perhaps in even larger measure (c) in countries now in need of development; that the long run effect will be to increase somewhat the amount of such development; and that the principal difference from the position that would obtain if no reparation were exacted, will be that the Germans will hold a smaller proportion of their own and foreign securities, while foreigners, particularly in reparation creditor countries, will hold a larger proportion.

"19. In the early years, no doubt, that part of Germany's production surplus which is devoted to reparation account may have to be, in large measure, invested in Germany, under the supervision of trustees for her reparation creditors. For the time this will present a considerable investment problem, for which, however, Germany's entire investment machinery can be utilized. If reasonable investment wisdom is exercised, a proper balance among various investments in Germany, and between Germany and abroad, can be maintained. As international confidence is restored, such securities can be absorbed by foreign private investors, individual and corporate, and government interests as such will diminish. In the meantime, such investments in Germany can be sound only in so far as they enhance the capacity of Germans and foreigners to absorb German goods.

"20. It is true that every extension of productive equipment in durable goods increases the opportun-

ity for miscalculation of future demand, for bad investment judgment, and hence for the recurrence, over a wider area, of industrial crises. But the reparation arrangement in contemplation strengthens this tendency but little, and it is in other directions that one must look for means to prevent, mitigate, or cure the evils which crises bring in their train.

"CONCLUSIONS:

"21. While admitting the force of Sir Josiah Stamp's conclusions, expressed in their final conservative form, my conclusion is that while certain peculiar problems will undoubtedly be presented by creating a surplus on reparation account which can not, at least in the early years, be currently withdrawn in full, the investment of this surplus in Germany will rather benefit than injure Germany's consumers, producers and economic organization, and that the process will operate in the direction of solving gradually the problems thus initially created, instead of magnifying them until a new type of economic calamity is at hand."

In his note number 6, Sir Josiah Stamp comments upon this matter. He sets aside as impracticable such tests for fixing indemnities, as "total cost of the war," "moral compensation," and "need of the Allies," and lays down as reasonable tests: the commensurate burden qualified by the necessity of modifying it by keeping it within the "physical limit of internal accumulation," and the "psychological limits of taxation" and applying it with due regard

to the "limit of exportable surplus." The importance of this last matter has been fully demonstrated, but it was believed that a way has been found to escape it, in part, by delaying transfers of wealth. He states that in his fourth note he had only hinted at the psychological limit but had discussed the matter of internal accumulation and the difficulties to be caused by it. He had received in response a note by Professor Davis so helpful and pertinent in criticism and suggestive in supplementary considerations that he appended it to his note for members generally to study. In his previous note he had said there was a great difference between raising a large revenue for internal use and raising a similar revenue for an ultimate external claim and the question to be considered is: are such differences and consequences likely to be injurious or helpful to Germany or the Allies? He proceeds to say that "psychological reaction comes earlier and lower than the limit of physical accumulation."

It must come for Germany at an earlier stage than in England where the whole payment by the taxpayer is directly beneficial to his country. The psychological reaction to heavy taxation is to discourage saving, to check enterprises and development, to lower the standard of living and retard growth of population by inducing emigration. He agreed with paragraphs 4, 5 and 6 of Professor Davis's note and with paragraph 7, that the surplus accumulation would be good for Germany up to a certain extent, and Professor Davis's points as to lower production costs and increase of goods and

free investment funds are undoubtedly sound, but this could not be carried on to an indefinite extent. The question is at what point will important reaction set in? Professor Davis suggests that the interest on the accumulations in Germany to outside creditors may never in fact be withdrawn, but the accumulation itself will tend to make the return on capital lower within Germany and there is no reason why people should in the long run make investments abroad. He agrees that the investments themselves will not leave Germany but some time the interest must be transferable.

He agrees with Professor Davis's remarks in paragraphs 12 and 13, but his comment that the balance between production for the present and production for the future would be adjusted naturally, if free play be given to economic forces, suggested the thought that an artificially induced balance is just what is being studied; and there is not free play to economic forces if there is any kind of unwillingness to receive German goods but a desire to postpone receiving them. The bonds could be freed at marketable rates only if full interest be payable at once and in such form as to be usable for the non-German purchases, so at this point the export surplus must be capable of transferring interest at least. Within moderate limits it could rightly be hoped that "the investment of the surplus in Germany will rather benefit than injure Germany's enormous budgetary and economic organization and that the process will operate in the direction of solving gradually the problems thus initially created."

But if it is agreed that the psychological limit is reached earlier than the limit of advantageous internal accumulation, it is not necessary to determine the precise limit of advantageous accumulation.

Mr. Francqui had stated that "it is known that Germany is almost the only European country whose commercial balance since the Armistice has shown, if not a constant surplus, at least a very slight deficit on the whole." But Sir Josiah Stamp regarded the following figures as the most reliable that had been submitted:

DEFICITS

1919	4.8 milliard gold marks
1920	1.9 milliard gold marks
1921	2.1 milliard gold marks
1922	2.2 milliard gold marks
1923	0.1 milliard gold marks

The above relating only to the visible imports and exports.

In a later note Mr. Davis submitted his ideas as to the possible use to be made of these accumulated funds to the credit of the reparation account, which in this connection will be found interesting.

"Subject: POSSIBLE APPLICATION OF WITHDRAWABLE BALANCES ON REPARATION ACCOUNT.

"1. If it should prove necessary, in order to protect the stability of German currency and exchange, to exercise restraint upon withdrawals from the reparation account in the German bank of issue, the balance on this account would tend to accumu-

late. Should such accumulation be permitted to continue indefinitely? Or should the balance, beyond a certain point, be withdrawn and separately invested in Germany?

"2. The bank of issue will have an interest in keeping this deposit down to small proportions, when it is not withdrawable. Deposits made on reparation account tend to swell the domestic assets (or reduce the domestic liabilities) while increasing what are essentially foreign liabilities. If the bank finds it difficult to transfer these balances to reparation creditors, it will also find it difficult to provide gold assets to serve as reserve against them.

"The reserve requirements are understood to apply to this balance as well as to other deposits and notes. Hence, the larger this balance, the lower the reserve percentage tends to be and the greater the bank's tendency to restrict domestic credits in order to prevent the reserve percentage from falling too low. Yet this restriction of domestic credits will presumably leave the bank with reduced holdings of ordinary paper and will force it to find other domestic uses for these funds. This it will have to invest in securities. Limited as it is in the choice of investment securities (since government securities are taboo) it may have to seek investments that are not generally considered suitable for a central bank.

"3. If the investment of large amounts should prove necessary, it is presumably sounder policy to put the responsibility for such investment where it belongs, namely, in the hands of representatives of the reparation creditors. In this way, the bank will

be relieved of the necessity of keeping reserves against balances that for the time are unwithdrawable, will not be forced to hold up its assets with investment securities, and will not be embarrassed in the performance of its proper functions.

"4. If such balances are to be invested on behalf of reparation creditors, how can this investment be managed? While it is probably unnecessary for the present committee to deal with this problem in detail, it is presumably desirable that the principle should be recognized. Hence a consideration of how it might be carried out is in point.

"5. Here a distinction should be drawn between that part of the deposit that is likely to be withdrawable in the near future, and that which probably can not be withdrawn for some considerable or indefinite period. The investment of the assets corresponding to the first part is essentially a banking problem, and there is no good reason for having it handled by any agency but the bank itself, since the sum will normally be loaned on short term commercial paper, or invested in other liquid assets. It would be undesirable for representatives of the reparation creditors to compete in such an operation with the bank itself. At most, it would be sufficient for these representatives to satisfy themselves of the quality of loans adequate to cover such a balance, and even this would probably be superfluous, under the present plan for the bank, if the deposit credit reached no large sum.

"6. The investment of the second part, however, would be an investment problem proper, as con-

trasted with a problem of commercial banking. Here the bank of issue has no peculiar advantage, and it would seem inexpedient to charge it with the responsibility of loading up its assets with the sort of securities that might properly offset the accumulating deposit balance.

"7. Probably the simplest procedure for the investment of this withdrawable balance would be to create a sort of investment company in which the Reparation Commission would hold the entire stock. The directors of this company would consist chiefly, if not wholly, of representatives of the reparation creditor treasuries, perhaps the same as those sitting on the subcommittees of the Reparation Commission, who would have to do with current withdrawals; but it might be advisable to have on the board two or three others, possibly including the comptroller of the bank of issue, provided the representatives of the reparation creditor countries should in any case constitute a majority of the board. To this company, the bank might turn over from time to time such sums as were for the time not withdrawable by reparation creditors, beyond a limited balance. The organization could be fairly simple or quite elaborate, according to the extent of the investment business involved, but it should be permitted to do no business except as an investor of these funds. It would naturally purchase sound conservative securities in Germany, thus contributing to Germany's internal development, her ability to render services (shipping, insurance, tourist, etc.) to foreigners, and her ability to export. Its

object would not be to earn the maximum possible return, but to invest safely in securities that could be readily liquidated. It would be subject to German taxation as applied to other similar concerns in Germany. Its earnings might be turned in to a special account at the bank with reparation creditors, subject to withdrawal in case the ordinary reparation account were fully drawn out, but otherwise diverted back to the company for further investment.

"8. The effect of this plan would be to interest the reparation creditors in Germany's internal development, to keep them in touch with Germany's financial situation, and to make them in effect and in some measure cooperators with Germany. If such funds tended to accumulate rapidly for a time, there would result a rise in the price of German securities, which by attracting foreign private investment, would increase the private flow of payments to Germany and so make possible the withdrawal of larger sums on reparation account.

"9. If in a certain period it proved that larger sums could be withdrawn from Germany than were available in either of the two accounts in the bank, this investment company could liquidate a portion of its investments and make the proceeds available to the reparation creditors.

"10. Conceivably, of course, there may prove to be no difficulty in withdrawing, from year to year, the deposit created in the bank by the government for the benefit of reparation creditors, or such balances as would accumulate might prove to be com-

paratively small. If so, the machinery suggested in this memorandum might be entirely un-utilized, or developed only in a very small degree, as needed. I believe it is impossible to prophesy how large sums can be transferred abroad without injury to the German currency and exchange. It will, in my judgment, be the wisest policy to contemplate machinery that may be unnecessary, rather than leave a possible contingency unprovided for.

"J. S. Davis."

The extent of the injury, if any, to be feared from the accumulation of an internal surplus in Germany or the difficulties to be encountered in transferring such balances into foreign exchange will depend, of course, upon the margin of government income over its necessary expenditures, out of which margin these funds are accumulated. Some better conception of what these sums will be, can be gained from a study of the figures submitted in the budget discussion. They will not at first be large, and as business becomes normal, the currency stabilized, and as a result production increases, the balance of exports over imports may increase as rapidly as the internal surplus.

February 20, 1924

After the Committee returned to Paris, Doctor Schacht came for another conference. The situation in Germany with respect to its currency and to credit for industry is critical, and Doctor Schacht will proceed at once to organize a bank, but upon such a plan as to render easy its amalgamation with

Joseph S. Davis

the new bank. In the interval this bank will issue its currency notes only in large denominations, against similar amounts of foreign exchange, and will grant credits to private industry, endeavoring to maintain the volume of gold and foreign exchange at 50% of total liabilities.

He is working in perfect harmony with his government and there can be no doubt that his bank will be authorized to do business at a very early date, and it is probably most fortunate for Germany that this step is being taken. There seems to be a complete understanding between him and the Committee, after long conferences as to details.

Some references have been made to these conferences. As his first appearance before the Committee Doctor Schacht made a statement which only confirmed the opinion of its members as to the precarious condition of German currency and credit. Immediate action seemed to be necessary to establish the temporary stability already attained, and immediate action could not be taken by the Committee, since it was their province only to report to the Reparation Commission. To wait until their report in all its details could be submitted, and the Reparation Commission could consider it, arrive at a decision and take the necessary action to make the plan effective, would be to invite disaster. But Doctor Schacht's plan, conceived as it was with the full approval of his government, could be put into execution without delay. The German Government urgently needed the application of some means of promised relief, as public confidence appeared to be

weakening. It approved the organization of a private bank to support the currency. The priority of reparation obligations was a hindrance to the action by the government itself.

The organization of a bank such as Schacht had in contemplation was a temporary measure only. It would require subsequent readjustment to conform with the general settlement of European controversies. At the meeting on February ninth in Berlin, Mr. Young made a statement accepted by the other members of the Committee to the general effect that he did not think that the Committee could assume the responsibility of preventing Doctor Schacht from putting his plan into execution. He fully understood that if Doctor Schacht succeeded, he might create conditions in Germany which would render more difficult the acceptance of the final plan of the Committee. But he did not wish to have the Committee find itself in the position of having prevented the Germans from utilizing their resources for maintaining an economic position achieved with such difficulty and held so precariously; because such a failure might result in precipitating the fall of the Rentenmark, and by thus hampering the movements of foodstuffs and raw materials lead to chaos in Germany. His chief concern was not whether Doctor Schacht's plan would necessarily avoid such a calamity. He wished to prevent the Committee from assuming the responsibility of placing obstacles in the way of Doctor Schacht's plan. He thought it preferable to let Doctor Schacht put his plan into operation, but to

make an arrangement with him whereby his bank might be absorbed by the bank proposed by the Committee in case the Reparation Commission should accept and carry out the recommendation of the Committee, and in accordance with this there was drawn up a statement for publication, which received the approval of Doctor Schacht after conference with the heads of the German Government and which reads as follows:

"The work of the First Expert Committee has enabled it unanimously to lay down the broad lines which it will recommend for the establishment of a new German bank of issue on a gold basis, which will exchange its own notes against those of the Rentenbank and the Reichsbank.

"The general principles of this plan have been communicated to Doctor Schacht, who is very clearly of the impression, shared by the Experts themselves, that if it is put into execution it will prove to be the most important step towards the definite stabilization of the German exchange and the balancing of the budget.

"The Expert Committee will inform the Reparation Commission that in its opinion the plan which the Committee will submit should be put into prompt operation.

"Doctor Schacht has informed the Committee that, in making his plan for the formation of his gold bank, he is so arranging matters as to facilitate its absorption by the bank of issue, which will be proposed by the Committee.

"The Expert Committee will meet Doctor Schacht on the eighteenth inst. at Paris."

In subsequent meetings with Doctor Schacht in

Paris, a careful examination was made of those features of his plan which were designed to facilitate the absorption contemplated, and it was agreed that the Reichsbank would use the voting power it would possess in the bank to be organized by Doctor Schacht to secure the consolidation of the Schacht bank with the new bank of issue.

The issuing on February tenth of the statement just given as to the harmony between the plans of Doctor Schacht and the Committee and indicating an intention to consolidate their efforts, undoubtedly had a strong effect in restoring confidence in Germany and strengthening the position of the Rentenmark.

CHAPTER VI

TAXATION REQUISITES OF A BALANCED BUDGET—PRELIMINARY BUDGET FOR 1924—CONTROL OF PAYMENTS FROM TAXATION BY INDEX OF PROSPERITY—OTHER SOURCES OF REPARATION PAYMENTS—PREVIOUS PROPOSALS OF GERMAN GOVERNMENT AS TO METHODS OF PAYMENT ON REPARATIONS—RAILWAYS OF GERMANY—IMPORTANCE OF RAILWAYS TO ECONOMIC AND MILITARY CONDITIONS OF NATION—OUTLINE OF BURDEN OF REPARATION PAYMENTS TO BE BORNE BY RAILWAYS—REVENUES FROM OBLIGATIONS OF PRIVATE INDUSTRY—OUTLINE OF AGENCIES TO INSURE PERFORMANCE BY GERMANY.

The balancing of a budget depends on maintaining the proper ratio between revenues received and money expended. Under normal conditions there is something anomalous in the expression "an unbalanced national budget." A nation can not spend more than its income, except by borrowing, and it can not borrow indefinitely to make up a shortage in taxation receipts, for it is such receipts alone that support its credit for borrowing. It must keep its expenses within its income and as a result there is among governments as much variation in the scale of expenditures as there is among individuals. But the extraordinary, abnormal and temporary expenses of war, require amounts far beyond the im-

mediate taxable resources of any country and under such circumstances, the present national income must be supplemented by borrowing upon the basis of the future taxation income of the government.

If the actual payment of these extraordinary expenses is thus spread over future years, there ought in theory, at least, to be no great additional strain upon money, and it ought to be possible to keep the currency convertible into gold at all times, and thus to check the rise in prices and hold them within the limits fixed by the increased volume of exchanges, rather than to remove all limit to the advance of prices by increasing indefinitely the supply of money through the issue of non-convertible promissory notes. To issue such notes is merely to avoid the issuance of bonds, by forcing the people to make a loan to the government without any assurance that it will be repaid at the same value. When a government adopts such a policy, it discharges its immediate obligations with a promise to pay at some indefinite future time a stated sum, the value of which is uncertain. It thereby balances its budget, but it corrupts its currency. For the future the fiscal needs of that government, not the state of commerce and credits, determine its monetary policy. When it needs more money to pay its expenses, it issues more currency, and thereby sooner or later depreciates the value of it, so that the rise of prices is aggravated, the expenses of conducting the government itself is increased, and a condition is brought about under which the balancing of its budget becomes a demonstrable impossibility.

A depreciating currency produces a shortage in the revenues of government for the simple reason that the taxes levied lose in value before they can be collected. Such a condition when long continued, destroys national credit, paralyzes industry, drives metal money and foreign credits into hiding, wipes out savings and investments, and deprives the people of the incomes out of which taxes must be paid.

Germany pursued no such policy as this during the years of strenuous warfare when all her resources were taxed to the utmost. Her fiscal problems at that time were solved without debauching her currency. It can not be believed that the burden of reparation charges alone made this necessary, for the aggregate paid while large, was still much less than her war expenses had been. But whatever was the origin of inflation and whatever caused it to run its full course, as it did in other countries as well as in Germany, it brought attendant difficulty in the balancing of the budget.

The recovery of Austria, reduced as she was by war, by dismemberment and by inflation, to the verge of starvation, would confirm the opinion that a sound and stable currency is the necessary condition of a balanced budget, and that with a stable currency, the budget may easily be balanced, but not necessarily upon the old scale of expenditures. But it must not be forgotten that the transition from a state of extreme inflation to a condition of stabilization is not an easy one. The adjustment of prices and wages creates a severe shock. The first effect is a great increase in prices, as measured by the gold

standard, without a corresponding increase in wages; a suspension of industry and a general crisis in credits. It was during such a period that we visited Germany. Credit was restricted to a painful degree but the stabilization to all appearances held, and improvement was already perceptible in the adjustment of prices and wages then in progress, and in the growing faith and confidence of the people. Nevertheless, a period of depression must follow such a crisis, and the development of normal ability to pay taxes will depend upon the restoration of activity in business and the building up of production.

The experiences of Austria might lead one to overestimate the recuperative powers of a nation, which has had such an experience; or a keen perception of the severity of the existing crisis might lead one to under-estimate them. In the midst of such conditions the estimates which must be made of the taxation income of the German Governments, federal and state, and of their necessary expenditures, are charged with much uncertainty.

Moreover there is an entirely new scheme of taxation and one to be applied by the Reich in some items which formerly were under the control of the states. These recent changes in the scheme of taxation and the disrupted conditions of business add to the difficulties of making the estimates. But the creation of a stable currency through the organization of a sound bank of issue will have a great influence in removing such uncertainties. Let the money system of Germany be sound and stable and so established

as to gain the confidence of the business world, in Germany and out of it, and the present depression will gradually disappear and be followed by a state of business activity and prosperity that will restore the tax-paying ability of the people and enable the government to make accurate estimates of its expenses, and to collect its taxes in money of unvarying purchasing power. At the same time it will restore the credit of the government, so that if the terms of the settlement permit, it can resume the normal methods of fiscal adjustment by making short time loans upon the basis of future taxation receipts to cover any temporary deficiency. Germany has been released from the burdens of past indebtedness by the depreciation of the mark and is thus relieved of what in the United States, France, England and the other Allied Nations is the largest item of their budgets, the interest on the public debts.

Assuming then, the stabilization of currency, the restoration over all the country of the full control of the German Government, the removal of economic barriers, and the cessation of large engineering projects of improvement, and it seems absurd to discuss seriously the mere balancing of the budget as a problem, for there is no problem and the only question is how much will be left, after balancing its budget, for the creditors of Germany. This seems to be the German view also, for the preliminary budget submitted in January, after due allowances for uncertainties, shows a substantial surplus of estimated income for the year 1924 over the prob-

able expenses of the government. And it is certain that these estimates are conservative.

In considering these figures it must first of all be assumed that the cessation of the Ruhr warfare will give Germany the taxation income from the occupied areas, and that German business will be relieved from the economic restrictions that have fettered it during the last year. It must also be remembered that a settlement along the lines of the Committee's plan, in itself, furnishes a great opportunity for the reestablishment of fiscal equilibrium and at the same time a large reward for its successful accomplishment, for there would be offered the extension of foreign aid for the organization of an adequate banking system to insure the stability of the currency, a foreign loan to meet immediate needs, the restoration of the economic unity of the country and a moratorium or material reduction of reparation payments during the period of greatest stress.

The following figures have been submitted to the Committee as the government's estimate of probable income and expenditure for the fiscal year of 1924.

(8) Finance and Taxation Departments..... 380

*Preliminary Survey of the Budget for 1924**

Revenue	In millions of Gold Marks	Expenditure	In millions of Gold Marks
1. General Administration of the Reich			
A. Ordinary budget			
(1) Taxes on property, traffic, trade and transfer (direct taxes)	4,004	(1) Interest on, and amortis. of debt of Empire	156
(2) Customs and excise duties (indirect taxes)...	1,080	(2) Provision for invalids, war pensions, etc.	810
		(3) Army and Navy.....	450

		(4) Police	208
		(5) Industrial and cultural purposes	28
		(6) Unemployment benefit...	500
		(7) Social and other expenditure	360
		(8) Finance and Taxation Departments	380
		(9) General administrative expenses other than the above	250
		(10) Assignments to the States and Communes..	1,800
(3) Non-tax revenues from Public Services	60		
		Total of ordinary expenditure	4,942
Total of ordinary revenues..	5,144		

B. Extraordinary budget

(1) Revenues from the mint	90	(1) For war damages and removal of effects of the war	6
(2) Other revenues	40	(2) Public buildings	44
		(3) Settlement of war expenditure	20
		(4) Settlement of expenditure for the Ruhr	60
Total of extraordinary revenues	130	Total of extraordinary expenditures	130
Total of A and B	5,274	Total of A and B	5,072

II. Execution of the Treaty of Versailles

(1) Cash Reparation Payments (discharge of debt due to the Reichsbank for redemption of an exchequer bill given to Belgium)	52
(2) Clearing Office payments	6
(3) Cost of Armies of Occupation	360
(4) Rhineland Commission	34
(5) Other Inter-Allied Commissions including Reparation Com.	18
(6) Restitution, substitutions and dismantlement costs	10
(7) Home expenditure incurred by the carrying out of the T. of V.	160
Total of expenditure	640

BALANCE:

Expenditure:	
I. General Administration of the Reich	5,072
II. Execution of the Treaty of Versailles	640
Total of Expenditures	5,712
Revenues	5,274
Deficit	438

*The figures of this table can only serve as a preliminary estimate and are given with all reserve. This estimate of the revenues assumes complete restoration of economic unity between occupied and unoccupied territory, renewed administrative and fiscal supremacy in occupied territory on the part of the Reich and the component states, that the taxes to be levied according to the general laws of the Reich and the states are once more directed into their treasuries.

The details of the first item of income amounting to four thousand four million gold marks as the proceeds of taxes on property, traffic, trade and transfer are as follows:

	Million gold marks
From the personal income tax	1,344
From the corporation income tax	144
From tax on capital	376
From death duties	210
From turnover tax	1,260
From taxes on transactions	440
From taxes on transports	230

The Budget Committee has been supplied with voluminous information and has pursued its work with amazing industry and care, and while they see chances for saving money in expenditures, and also dangers of a shortage in some items of estimated expenditure, they agree that in all probability one will offset the other, and that there is every probability of the accomplishment of at least the results that are tentatively forecast. There is no danger of a shortage that would endanger stability of the currency, or that would be so large as not to yield easily to the usual fiscal devices, such as increasing the floating debt, or making short term loans, or by increasing certain taxes under emergency.

Some brief discussion of the items of this budget may be interesting. Of the personal income tax, eight hundred sixty-four millions are anticipated from the tax on salaries and wages and four hundred eighty millions from the incomes derived from agricultural, industrial and mining undertakings and

from interest and dividends and from professional earnings and from the super-tax on large incomes. The first estimate, that on wages and salaries, has been made upon the general assumption that the number of unemployed would remain at three million, which it was at the time the budget was prepared and that the average wages would be four gold marks per day. As this number decreases, the income tax collected increases and the expenditure for unemployment benefits is reduced. The number of the unemployed in November rose to four million. It is perhaps not perfectly safe to assume it will fall much lower than three million, but as conditions have improved and seem to be improving, there is every reason to believe it will continue to decline. And as for the second item of four hundred eighty million marks, upon the income from personal activity in business, it is, of course, extremely low, but it is assessed not upon the profits actually earned in 1923, but upon presumptive evidence of past earnings. The profits of 1923 were made in depreciating marks, which eventually lost the greater part of their value. The tax in 1925 will be levied upon the earnings of 1924 and as to this particular item ought to show a great increase.

The rate of death duties is regarded as being less than that prevailing in other countries of Europe and should be materially increased in future years. The turnover tax of 2½% is levied upon every sale, and upon some articles several times, as they are used in manufacturing other articles, or sold from manufacturer to dealer and to retailer and to the

user. The estimated yield of one thousand two hundred sixty million marks also seems to be conservative and postulated upon a continuing state of depression. The one and one-tenth per cent. tax of a similar nature in France, but not applicable in that country to agriculture, produced in 1923 three billion francs. Upon the same volume of business a two and one-half per cent. rate would have produced in France six thousand eight hundred million francs, or at four francs to the gold mark, about one thousand seven hundred million marks. The estimate that the gross business turnover in Germany with a population of sixty million would be slightly less than that of France, with a population of forty millions, seems conservative and on the safe side.

The taxes on transactions, estimated to yield four hundred forty million marks, contain the large item of one hundred fifty million marks of taxes on transfer of land, sixty-two million on stock exchange transactions, fifty million on automobiles and trucks, sixty-five million on bills of exchange and are accepted as being, in the aggregate, safe to rely upon. And the total aggregate of the direct taxes, four thousand four million marks, is also believed to be safe, though many variations from detailed estimates are expected.

The tax on capital (three hundred seventy-six millions), corporations income tax (one hundred forty-four millions), and on personal income (four hundred eighty millions), an aggregate of one thousand million marks is the total estimated yield from all incomes, other than the incomes from wages

and salaries, which is estimated at eight hundred sixty-four millions. Even this latter figure seems low since it is based on the assumption of a continuation of excessive unemployment and a low rate of wages, but the ratio between this and the tax return upon all other incomes can only be excused by the assumption that circumstances for the moment prevent the application of an equitable tax in 1924 on the incomes earned in 1923. With any real improvement of business these taxes ought to yield much more than these estimates, and the tax on all other incomes ought to be very much larger than the tax on wages and salaries.

One large item of customs and excise duties, total one thousand eighty million gold marks, is customs or taxes on imports one hundred sixty million gold marks, which compares with the pre-war figure of four hundred millions; and it was also calculated that the application of rates now prevailing in Belgium would produce six hundred million gold marks. This estimate includes no tax on agricultural products, and the farmers are demanding a duty on cereals, which may become effective. The actual yield is likely to be larger. Another large item is the tax on tobacco (three hundred sixty million gold marks). It is based on a consumption of nineteen billion cigarettes, which is regarded as low, and the rate is from 20% on ordinary pipe tobacco and cigarettes to 40% on the better grades; and the tax on sugar (two hundred thirty-two million gold marks) and on beer (one hundred twenty-six million gold marks) and spirits (one hundred twenty mil-

lion gold marks) are all based upon very low estimates of consumption. In any prosperous year the yield from these sources would be greater.

In a general way the estimates for expenditures have been controlled by the same fundamental assumption of continuing depression, being based upon the present state of unemployment. The crisis occasioned by the change from a depreciated currency to a gold basis was really precipitated in November. It has lasted more than two months and the movement of prices indicates improvement. Unless a disturbance of the stability already established occurs, it is certain that this experience will be followed by a resumption of business activity and the very great reduction of unemployment. This will affect both sides of the balance sheet favorably. The income from all taxes will increase and especially those on salaries and wages, and other incomes, and at the same time there will be reductions in some of the large items of expenditure. For instance, the items of unemployment benefit (five hundred million gold marks), war pensions (eight hundred ten million gold marks) and social and other expenditures (three hundred sixty million gold marks) would be reduced by a return of prosperity.

Then there are the items for the army (three hundred forty-eight and one-half millions) and the navy (one hundred one and one-half millions), which have come under some criticism. The Treaty limits the numbers of the army and as a matter of fact the salaries are not excessive. The old army was one

of conscription and the present one is paid. The old army was of about eight hundred thousand men with mobilization equipment for about four million. The present army is of one hundred thousand men. The expenses of the army for 1913 is compared with the estimates for maintaining the new army of 1924, as follows:

	1913	1924
(1) Training	11,816,000	6,240,000
(2) Quartermasters' service	6,319,000	3,055,000
(3) Arms material arsenal.	86,212,000	56,208,000
(4) Clothing	54,154,000	23,544,000
	158,501,000	89,047,000

The estimated expenses of maintaining an army 12½% of the size of the old army are nearly 60% of the expenses of the old army, on just these items.

The doubtful item of this budget is probably the one thousand eight hundred million marks set aside for the states and communes. There is probably the need and demand for more for this purpose, and had the expectation been for higher gross revenues, more would have been assigned to the states and communes. This was an influence toward moderate estimates of income on the part of the government. Great expectations of receipts would have brought greater demands from the states and communes; and upon the other hand it probably was felt by the members of the Committee that estimates, from their standpoint, ought to be moderate, since in all probability some credit must be sought to take care

of the claims of Germany's creditors, and the assurance of improvement in the general conditions of the country depends so much upon the fiscal balance sheet of the government that the greatest care must be taken not to hold out any false hopes of immediate and complete recovery of the ability to balance the budget and provide a surplus. Although the Reich is charged with the administration of some of the taxes formerly collected by the states, it is under obligation to see that a portion of the proceeds of such taxes is turned over to them. There is no clear distinction between the functions of the Reich and the state governments, nor as to the claims of the latter upon revenues, which creates a great difficulty for those who are charged with the administration of the finances of the Reich. To some extent this confusion existed before the war and must have been largely overcome during its conduct. But Germany as a whole must bear its financial responsibility to the creditor nations of the world, and this responsibility can not be evaded by any distribution of constitutional authority among subordinate states or constituent parts of the country.

The population of Germany is about sixty million and these figures forecast the ability on its part to raise revenue this year just sufficient to meet the costs of administering the government. Great Britain with forty-eight million population must do the same, and pay interest upon about seven billion five hundred million pounds; France with forty million population must, after meeting its expenses of administration, pay interest on about four hundred

fifty billion francs; Italy upon one hundred eighty-six billion seven hundred million lira; and the United States upon about twenty-one billion dollars. It would seem, by comparison, that eventually Germany could also raise very substantial sums in addition to the amounts required to administer its government. Or to make a comparison upon another basis—the budget we have been considering is that of the Reich, and state and municipal taxation will add about three billion marks making a total for Reich and states of about eight thousand two hundred forty million marks. Let us assume that this tentative forecast is correct and the budget balances except as to the expenses of Treaty charges, and let us assume the necessary expenses of the government increase by 20% on account of conditions and tendencies referred to. We have then nine thousand six hundred eighty-eight million marks as the total taxation burden of the German Reich and states for internal expenses. If the sum of one thousand two hundred fifty million marks be added for Germany's creditors, the total tax burden becomes ten thousand nine hundred thirty-eight million marks. Assuming the population by 1928 to be sixty-four million, the per capita total tax burden would be one hundred seventy-one gold marks or the equivalent of about forty-three dollars.

This sum seems low when compared to our own taxes, but we have not had such experiences as have within recent years reduced the tax paying capacity of the German citizen, and all of the money we pay in taxes remains within our country and is returned

to us in facilities and improvements and without any subtraction from our national wealth. Whereas in Germany, the destruction of savings and investments of great classes of thrifty and industrious people, and the wiping out of working capital adds immeasurably to the burden of paying taxes. A portion of the taxes paid must be sent out of the country also, thereby reducing the national assets. All things considered, this burden has been considered commensurate with the burden of other nations. It will be, however, only slightly greater in aggregate amount than it was in 1913, for then it exceeded ten billion marks. But in 1913 it was all expended within the country, whereas under the plan proposed, 12% of it, besides an equal amount out of the earnings of private property, would have to be sent beyond its territorial limits, and without producing any direct beneficial result other than the cessation of present intolerable conditions.

If a system of control should be established whereby expenditures were to be held to the lowest point consistent with the maintenance of government, there would not be much inducement to the people to submit to stringent tax exactions merely to increase the amount of payments to be made to foreign creditors. As the gross amounts of taxes paid increase, the benefits to be extended by the government to the people ought also to be enlarged.

It is regarded by all as necessary both to leave the maximum of freedom to the German Government to control its system of taxation, and also to permit the Germans to share in the proceeds

Reginald McKenna *at right*
Chairman Second Committee of Experts

of taxation beyond some fixed normal rate of aggregate tax collections, and to receive progressively a larger proportion of the surplus accruing over expenses. But if Germany spends more money in administration, as she feels her tax revenues and prosperity growing, she must also spend more money in paying her creditors. Such has been the demoralization in Germany that it is not to be expected that this fixed normal rate of tax-payments could be attained for four or five years. The budget for 1924 is really regarded as likely to be balanced and the 1925 budget is expected to show an improvement of between five hundred million and one thousand million gold marks over that of 1924.

A normal year would hardly be expected before 1927 or 1928, and although it is expected the gross collections for taxes might then be sufficient to provide two billion marks for interior payments, there is a disposition not to suggest a compulsory minimum amount of payments of over one and a quarter billion marks from the budget surplus, and this amount has been suggested as the normal payment.

But with this surplus of one and one-fourth billion marks as the standard normal rate of accumulation to the creditors of Germany after 1928, some scheme for automatic additions to this minimum amount ought to be provided in order to allow Germany's creditors to share in her increasing prosperity. The mere amount of increased taxation income is not believed to be a conclusive measure of her ability to increase payments to her foreign creditors. It is one test, for almost any of the taxes

we have been considering would show a higher yield in prosperous times than during a depression—the income taxes, the taxes on gross sales, and the taxes on exchanges, especially. But on the other hand, the government may choose to raise less revenue than it would if no outside obligations existed, and taxes might be shifted by the Reich to the states. In general, taxation income is not a fair criterion of prosperity and to make it the sole test might repress beneficial expenditures and in some measure delay economic development. Nor is the total volume of exports by itself a fair criterion, though at the present time by the tax of 26%, to some extent it serves as such in theory only. Rather than to retain this it was considered more rational to draw up some index of prosperity and to increase the demands for payment beyond that regarded as the minimum, say one and one-fourth billion marks for the normal year 1928, in the proportion that the index records increasing prosperity. To prepare such an index is a complicated problem, to solve which there are present at this conference some exceptionally well qualified men, the most competent of whom is Sir Josiah Stamp, Chairman of the Budget Committee, whose sound judgment and untiring industry are of incalculable value. Much study has been given to this problem, and the final result may be found in Annex 2 (page 417) of the Committee's Report. It is suggested also that the German Government and its creditors should have protection against any serious fluctuation in the general purchasing power of gold as compared with the year 1928.

The point of contact between the Committee and the German Government established at Berlin has not been broken. There has been continued correspondence and the representatives of the German Government have been in Paris at different times for conference. The scheme being worked on is subject to change and no one except the members of the Committee themselves know the exact status of present agreements, and, of course, not even they know the exact form it may eventually take. But the foregoing is an outline of an adjustment that has received tentative approval. The payments outlined, together with those to be described later, include all payments arising from Treaty charges and all payments in fact upon Germany's obligations to the Allied and Associated Powers. From a consideration of Germany's condition, it is believed she could not safely make any payments from her current budget income during 1924, but could make moderate payments in subsequent years up to 1928, when the sum of one and one-fourth billion marks might be raised by Germany through taxation, to be applied upon her foreign obligations, and after that more according to the increase of her prosperity, and these amounts were considered to be all that Germany could pay whether in cash or goods, and without regard to the claims against her upon which the payments were to be made, whether for reparations, expenses of Armies of Occupation, or any other Treaty obligations.

The sums which the Committee believes Germany can safely provide and ought to be required to pay

out of her taxation income upon her Treaty obligations are: for 1924, nothing; for 1925, two hundred fifty million gold marks in which year a special provision to be described later, is made; for 1926, one hundred ten million marks; for 1927, five hundred million marks; and for 1928, one thousand two hundred fifty million marks. But these sums do not meet the necessities of Germany's creditors, nor exhaust the resources of the German nation that might be applied to the payment of its obligations. There is a possibility of larger payments from its taxation income and also the opportunity to utilize for payments certain valuable property owned by the government and other properties privately owned, but justly subject to the demand that it be devoted in part to reparation payments.

The whole system of direct taxation went to pieces in 1923 and for that reason and on account of the confusion occasioned by the inflation there was a very low scale of taxes upon the incomes of very rich men; and this condition is necessarily thrown over into 1924. But as soon as recovery takes place and profits may be measured in a stable currency, these large incomes in Germany should be subjected to taxes as severe as those which are being imposed in other countries. There is an especial reason to support the justice of such taxes in Germany, which does not exist in other countries, namely, that the depreciation of the mark has in a particular manner inured to the benefit of the very class of men who being actively engaged in business, are in possession of large incomes. The great profit that has been

made by the wiping out, through depreciation of the currency, of the entire indebtedness of large corporations or of large business men, is itself a suitable subject for taxation in such an emergency, because such a tax would fall on those who are demonstrably able to meet it and because whatever is taken from them by this sort of a tax is in fact the recovery of a part of what has, through no intent of their own, been taken by them without compensation from others.

The wiping out of bonded and mortgage indebtedness, the profit made by repaying in depreciated currency the credits granted by the banks, and the payment of taxes in money of depreciated value have resulted in great accumulations of unearned wealth in the hands of a relatively small number of German business men. German authorities have estimated the total mortgage debt encumbering agriculture before the war at the minimum figure of fifteen billion marks, and industry, as well, has been freed from a great but not easily ascertainable burden. The German Government itself considered the utilization of these abnormal profits for the payment of reparations. In a memorandum submitted on June 7, 1923, to the Allied and Associated Governments, it expressed itself as follows:

The German Government propose the following as a part "of a definite reparation settlement" (b) to secure a further annual payment of five hundred million gold marks as from July 1, 1927, the German Government will at once subject the entire business, industry, banking, trade, traffic and agriculture of

the country to a guarantee in the form of a first mortgage of ten milliards gold marks on real estate whether buildings, dwellings, lands or forests. The annual dues of five hundred million gold marks will be levied either indirectly in the form of a general tax on all classes of property or on the specific objects of the mortgage.

This proposal by Doctor Cuno's Government was subsequently several times confirmed by the successive governments. The Committee has, therefore, been considering the means for mobilizing the mortgage on industry and agriculture, which the German Government has thus offered to constitute for the benefit of its creditors. The suggestion is that the German Government should subject a portion of these assets to a new mortgage for the benefit of its creditors in the sum of five billion marks. All the mortgages on industrial undertakings will be secured by indentures whenever the capital exceeds one million gold marks, all other mortgages to be entered in the legal form of the German land register; all bonds upon such property placed in good faith prior to April 1, 1924, to be protected in their priority over this issue; the bonds thus created to bear no interest the first year, 2½% only on the second year and 5% the third and following years, and to be due in forty years and redeemable at any time out of collections made from owners of property who wish to discharge the mortgage obligations against it.

After full consideration and a careful study of the best way in which to handle this valuable re-

source to the best advantage for Germany itself, as well as for its creditors, it was decided that a mortgage debt to the amount of five billion marks on the industries of Germany, fairly apportioned by the German Government, payable at long maturities, would not create a heavier burden than that which would have existed had there been no depreciation of the currency. At the same time it is suggested to the German Government that a discriminating burden upon the large industries for the benefit of Germany's creditors ought not to be exacted, but that a source of income might be available for the uses of the government by equalizing the burden over all industries, large and small, and over agricultural and real estate interests as well. For the Committee has decided not to demand what the German Government offered in its note of June 7, 1923, with respect to a mortgage upon the real estate of Germany. Realizing the importance of agriculture to a nation unable to provide its entire food supply, and the great importance to any government of an unhampered relation to its agricultural interests, it has refrained not only from asking that a mortgage should be placed upon the real estate of Germany for the benefit of its creditors, but also from making any specific suggestions as to the manner in which Germany should use this asset. It has, however, besides suggesting the equalizing of the burden over all interests in Germany with that to be laid upon industries, indicated its opinion that a large amount of agricultural indebtedness has been discharged at merely nominal figures and that the

owners of equities in lands have realized substantial profits at the expense of former creditors, and that as a result of this, the government might, with justice, find a new source of revenue. The manner in which this arrangement may be carried out is more fully described in the "Plan for Industrial Debentures" which may be found in Annex No. 5.

The income to be derived from these bonds would be: in 1924, nothing; in 1925, one hundred twenty-five million gold marks; in 1926, two hundred fifty million gold marks; and thereafter both the full interest of 5% and the amortization of 1%, or three hundred million marks. The payments to be made out of the budget must be provided by the taxpayers of Germany, but the payments to be made from the interest on these industrial bonds lays no direct burden on them but creates a relatively small burden on those specific industries which have benefited in a substantial manner by the misfortunes of the nation. Both payments are of equal value to Germany's creditors, but of unequal weight on the German taxpayer and of very different economic effect within that country. The industries which will carry this burden to the great relief of the taxpayers will not have an indebtedness so great as that which would have been carried by the same organizations had no depreciation taken place.

The Committee having suggested these specific payments, the first up to the limit of what ought in their judgment to be laid upon the taxpayers of Germany, and the second, that which ought to be made by specific industries, have proceeded to the

examination of another very large asset out of which payments might be secured, that is the Railway system, now the property of the Reich.

In the same memorandum of June 7, 1923, to which reference has already been made, the German Government proposed (a) the detachment of the railway system of the Reich to be held in separate fund, obligations to be issued, having a first charge on its earnings in the sum of ten billion gold marks, bearing 5% interest. This suggestion commends itself to the Committee, for it will be another source of large collections that must be carried by private property, without its being felt as a burden by the taxpayers for the reason that the German Government has never received an important income from its railway system. The surplus earnings have heretofore been reinvested in the property itself.

This system of railways, having a replacement value of more than twenty-five billion marks and an earning capacity under favorable circumstances of one billion marks, with freedom from important obligations in the form of indebtedness, is obviously well adapted to supply the credit necessary to meet the necessities of Germany's creditors during the period of Germany's recuperation, within which time no important payments could be made out of her current income. The railway system, and the manner in which it could be used as a medium for reparation payments, is a subject so important and interesting as to require a somewhat extended discussion of the manner by which additional payments may be secured from this great asset of the German

Reich. And when we have ascertained what payments may be expected from this source we can, by adding to them the payments from the budget receipts, and those from the industrial bonds, have the total amount to be paid by the German Nation from its taxation income and from private property devoted to the purpose of discharging its foreign obligations. That portion which is to be carried by private property will be evidenced by bonds, not such as the A and B bonds, which were, to some extent, mere accounting devices, but bonds secured by specific indentures and sustained by actual values and earning capacity, and these bonds when sold, either to Germans or the citizens of other nations, will be purged of political complications. They will then become the obligation of private companies or of the German railway system, to individuals in Germany, and out of it, and thus be freed from the appearance of being a part of the war indemnity.

A full discussion of the condition of this system of railways made by Sir William Acworth and Monsieur Leverve may be found in Annex No. 3 and is of great interest.

The railways of Germany are, or in the end will be, a very important factor in making the final adjustment, because of the variety of relationship this system sustains to the government, to the domestic and foreign business of the country, to the safety of armies of occupation and to the raising of revenues for the purposes of government. The system belongs to the government; it has no bonded debt

and if consolidated into one operating unit will be probably the largest one in the world. The operation of this system in the past has been by the government, and actuated by political motives or a conception of the public interest, rather than only by the business interests of the system itself. It was used to encourage by heavy rebates the sale of German goods abroad; it was an important part of the machinery by which the "dumping" so much resented by the business men of other nations, was accomplished. While it may be improbable that big business would continue to receive such favors from the present German Government, it nevertheless would probably not be acceptable to the business men of other nations that such a power should be left unrestricted with the German Government during the difficult period of readjustment which they are all facing.

The great value of the system, its entire freedom from bonded debt, the large earnings to be derived by careful management, and the fact that it has not heretofore contributed in an important way to the German budget, make it available for use in the payment of reparations and especially because sooner or later, and in large amounts, bonds may be sold and the proceeds used directly for reparations. This provides a strong motive to establish good working conditions and the maximum of profits. Its proper operation moreover is necessary in order to establish productivity in Germany, without which the prosperity of her neighbors is threatened and the hope of reparation payments withdrawn.

It is clearly brought out in the joint report of Monsieur Leverve and Sir William Acworth that the interests of the Allies, as well as Germany, require that the system should be operated as a unit and without any restrictions as between occupied and unoccupied Germany. Without raising the question as to whether political conditions in both France and Germany compel the continuation of some military restraint, the necessity for the removal of economic restraint is apparent, at least such restraint as in the past has prevailed. The whole question of control and how it should be exerted by the Allies over Germany really centers round the railway system. The control of it means the control of Germany and no army of occupation could establish a control without taking over the railway to insure its supplies.

In compliance with the Versailles Treaty (Article 212) the German railroads in occupied territories were controlled by the Commander-in-Chief of the Allied Armies and this control was carried out through the medium of the Inter-Allied Commission of Field Railways, which body has a representative of the Minister of Communications of the Reich at its disposal. The German railways were bound to carry out all orders given with military purpose and to supply statistical information as requested. The administration and financial management was left in the hands of the Reich. In case a state of siege should be declared, the railroads were to be entirely under the control of the Commander-in-Chief. For a time this system worked very well, but after the

occupation of the Ruhr and the beginning of passive resistance, the order issued by the Reich to all railroad men of the occupied territories to quit work, compelled the Commander-in-Chief to place the roads under military operation, and for this military operation the so-called Franco-Belgian *régie* was substituted after a period of two months. The refusal of the British Government to have its zone of occupation included in this *régie* has introduced another zone of operation and an additional complication.

The *régie* operated the roads of former occupied territories (except the British zone) and the railroads of the Ruhr. Considering the fact that this *régie* took over the operation of the railways as the direct result of the order of the German Government to establish a general strike, it was hardly to be expected that the roads would be managed in a manner to meet the demands of German commerce. It was, in fact, a strong weapon in the hands of the Allies in the war of passive resistance. The traffic between occupied territory and unoccupied Germany is barely one-sixth of what existed prior to the Ruhr occupation so far as the Frankfort Railway district is concerned, and it is probable that the same ratio prevails in other districts. There are delays in the mails, difficulties in securing passports from unoccupied into occupied Germany and hardships of travel imposed. Moreover a system of requiring permits for shipping goods into occupied territory has greatly obstructed business, but most serious of all, French goods are shipped into Ger-

many with preferential tariff charges or without any customs duty. This so-called "open hole" has had disastrous effects upon the whole commercial system of Germany. The Germans have bitterly complained of these things.

Having now ceased the passive resistance and withdrawn the general strike order, they hope for, and ought to receive, as soon as possible, release from the Franco-Belgian counter-offensive against the measure of passive resistance. It is imperatively necessary to remove these obstructions to commerce; it is the first requirement in order to restore the productive power of Germany, but it can hardly be expected that this control established by France and Belgium at such a cost would be at once entirely withdrawn upon the mere promise of Germany to accept a general program of settlement. It seems to be a general opinion that to terminate abruptly the military control would not be politically possible from the standpoint of France nor necessary from the German standpoint. The decision of this matter rests with Allied Governments. But if economic pressure over the railways is to be released and military control over the occupied areas to be maintained, whether in the Ruhr district or in the territories set out in the Treaty for occupation, it would seem to be a fact that sufficient control over the railways would have to be continued to insure the safety of the transports of the armies of occupation and the carrying out by Germany of its agreements, and possibly to prevent another arbitrary strike upon political pressure, and especially for the

protection of Allied interests in the revenues from the railroad system for reparation purposes.

This need not involve the maintenance of large forces nor the taking over the management of the roads. It could be placed in the hands of some board, the activities of which would be limited to the gathering and publishing of statistics and to the general observation of the operation of the roads, until such a time as some dispute might arise as to whether agreements were being carried out. In case they were not being carried out, this board, under conditions set forth in their organization, could take over and operate the railways. At least it appears that some assurance must be given that under all circumstances the railways should be operated as a unit and as the servant of commerce and not as a weapon in commercial warfare, nor as an agency for unrequited social service.

The matter of the control of the railway system is one of the most vital importance, both to German revival and Allied interest. It is the asset of greatest value for reparation payments and also the essential means for the support and protection of troops so long as any measure of military control is maintained. And from the German standpoint its unified and unobstructed operation under the most efficient management is necessary to reestablish and sustain the prosperity of business and the peace and comfort of the people.

It is proposed that a private company be organized to take over and operate the German railways under a law which being approved by the Repara-

tion Commission will be adopted by the German Government, which shall embody a contract between the company and the government, of which the following shall be some of the terms: The company will be of German nationality, and will operate the railroads with power to fix tariffs, but without discrimination, so as to yield a return sufficient to pay interest on bonds and dividends on preferred stock and a reasonable return on the common stock, and the power of the German Government to control rates will be limited to those set forth in the contract, and no new direct tax upon the property or business shall be levied. The term of the concession shall be at least fifty years at the end of which period, the company will return to the German Government the control and possession of the property, providing the charges against it have been met. These charges are determined by the bonds to be issued and by the transport tax.

This company will be administered by a board of at least eighteen members, half to be appointed by the German Government and half annually by the trustee for the bond-holders, and of the nine members appointed by the German Government four at least will represent the holders of preferred stock and of the members appointed by the trustee five may be German nationals. The Chairman of the Board will be one of the German members representing shareholders, and will have a casting vote and shall be elected annually. The business of the Company will be conducted by a general manager of German nationality. The foreign members of the

Board shall select a commissioner, who shall not be a member of the Board, and shall be a person accepted as being in the first rank of railway men. This official shall have the right of inspection for himself and staff, and shall receive all reports and returns, proposals for extensions or tariff changes and everything of such a nature as to require the attention of the general manager and will be entitled to call for any other reports, returns or statistics, such as he may consider necessary in order to enable him to form an independent opinion. In case of disagreement as to policies of management between the commissioner and the manager, it shall be submitted to the Board of Management. If the property fails to realize the net receipts necessary for interest on the bonds, the commissioner shall have the right to take such action as the trustee for the bond-holders and the foreign members of the Board may consider necessary to protect the rights of the bond-holders, including the right to operate, lease or sell the railways in whole or in part.

The company shall issue to a trustee to be appointed by the Reparation Commission first mortgage bonds to the amount of eleven billion gold marks, bearing interest at 5% and 1% for a sinking fund. The payment of these bonds shall be guaranteed by the German Government. From and after the fifth year, the bonds shall be amortized under conditions to be determined by the trustee, by the application of the annual payments provided for, or by such additional sums as the German Government may furnish for the purpose. These payments are

specified as follows, to be made from the gross receipts of the company before ascertainment of net profits:

(1) The amount of the transport tax, estimated at about two hundred fifty million marks, which may be employed by the trustee to secure a special issue of bonds.

(2) A sum sufficient to secure the interest on the bonds. But the bond-holders will accept on account of interest in the first year three hundred thirty million gold marks, the second year four hundred sixty-five million gold marks, the third year five hundred fifty million gold marks and in the fourth and subsequent year six hundred sixty million gold marks.

The Reparation Commission shall be entitled to divide the bonds in any manner it may think expedient into different classes with varying rights or to issue debentures against the deposit by the bonds or any part of them. The Company shall not be able to issue other bonds than these without the authorization of a three-fourths majority of the Board, of which majority two must be foreigners. There shall be thirteen billion gold marks of common stock, and two billion gold marks of preferred stock. This preferred stock will be sold by the company and three-fourths of the proceeds will be used by the company and one-fourth will become the property of the German Government, and all of the common stock will belong to the German Reich. The details of this organization may be found in Annex No. 4.

It is not probable that divisible earnings will accrue to the common stock, but the continued payment of six hundred sixty million gold marks annually toward interest and amortization of eleven billion five-per-cent. bonds will discharge the bonds in less than fifty years, and as the bonds are discharged the common stock increases in value, and ultimately the entire property will revert to the German Government. So far as these railway bonds are concerned, the position of Germany would not be much different from that of the United States Railways, at least until very recently. Upon the actual value of its railways, Germany would be paying about 2½% in interest and amortization for about fifty years. Very roughly speaking, since most of our railways have been built from the proceeds of bonds sold abroad and in amounts almost equal to their actual cost, it is probably true that for many decades there was sent abroad for the payment of interest as large a percentage of the cost of our railways as this. During recent years this railway system has been a burden on the German taxpayers, for in the readjustment since the war its operation has resulted in losses.

The Committee recommends that a transport tax of seven per cent. upon the gross revenues of the railways be imposed for the benefit of Germany's creditors, but in effect provides that this tax may be used by the German Government for its own needs for the years 1924 and 1925. The estimated income from this source for 1924 is two hundred fifty million marks. After 1925, the proceeds of this

tax will be paid to the reparation account, until it amounts to two hundred ninety million marks which is expected in 1926. After that the excess over two hundred ninety million marks may be retained by the German Government. The proceeds of this tax may be employed by the Trustee to secure the issue of another series of bonds for three billion marks. The payment of this tax to Germany's creditors shall continue during the period of the concession of the railway property to the company, and this period, it is specified, should be of sufficient length to allow of the amortization of the eleven billion bonds.

The payments to be expected as a result of the general plan of the Committee so far as explained, and especially the payments of 1924 and 1925, do not afford the assurance of necessary relief to the creditors of Germany. There are expenses of armies of occupation in 1922 reported to us as being one hundred sixty-one million marks, and in 1923, one hundred fifty-five million marks. In the budget just examined the expenditure for 1924 was estimated at three hundred sixty million marks. The Committee makes it clear that the sums they name for future payments comprise all amounts for which Germany may be liable to the Allied and Associated Powers, including reparation, restitution, all costs of armies of occupation and commissions of control or supervision, and that payments made in goods are to be placed to its credit upon the same basis as payments made in cash.

But the business relations in Europe have become

Monsieur Jean Parmentier
French Member First Committee of Experts

adjusted to the system of deliveries in goods of commerce such as coal and its derivatives, timber, etc., and these can not be terminated without injury. In 1922 the deliveries in kind were six hundred eighty-one million marks and in 1923 (the Ruhr not included) four hundred sixteen million marks. The demand for deliveries of goods in kind may be between five hundred million marks and seven hundred fifty million marks, but such estimates are uncertain for there is at times a difficulty in accepting, as well as making, such deliveries. What is taken in such forms reduces what may be taken in cash and the effect of this condition may be to reduce both the expenses of armies of occupation and the demands for deliveries of goods.

To meet the necessities of creditors while at the same time taking every precaution to protect the solvency of Germany, the Committee proposes a foreign loan upon the security, assuming the consent of the Reparation Commission and the Allied Powers, of a first claim upon the German revenues and in the sum of eight hundred million marks. This loan would both provide for the financing of deliveries in kind and be a source of strength to the bank and the general credit conditions of Germany. For the proceeds would be deposited in gold or gold exchange in the bank, and the government would make its payments in connection with deliveries in kind in its own currency and in bank credits. The gold reserve of the bank would be increased, and if desired, made the basis for an increase of currency. This credit would come to the bank at the very time

it would be most needed. The proceeds of this would be the bulk of the payment to be made in 1924. The Committee suggests as a further precaution that the proceeds of the foreign loan should all be expended within Germany in payment for deliveries in kind and for the expenses of the administrations created by the Allies. The loan is considered an integral part of the plan, as being essential to the successful establishment of the new bank and for the stabilization of the currency and the restoration of credit and working capital. The credit established by the loan is in gold and gold exchange; the proceeds of the loan must be expended within Germany. There is thus provided the means for meeting the immediate and urgent need of the Allies in so far as they can be supplied through the furnishing of goods and without necessitating the transfer of money abroad. In addition to the eight hundred million marks secured from the loan, it is proposed that only two hundred million marks should be demanded as interest on the railway bonds during 1924, and that the interest payment in 1925 on these bonds should be increased by the same amount, as the 1924 payment is reduced, namely—one hundred thirty million dollars. The 1925 payment would then be five hundred ninety-five million marks.

Assuming that the five hundred million marks of preferred railway stock should be sold in 1925, the annual payments in millions of marks may be expressed in the following table:

	Budget	R. R. Bond Interest	Transport Tax	Industrial Debentures	Sale of Securities	Total
1924	....	200	...	...	800	1000
1925	....	595	...	125	500	1220
1926	110	550	290	250		1200
1927	500	660	290	300		1750
1928	1250	660	290	300		2500

If it should happen, however, that the railway preferred stock could not be sold in 1925, then the transport tax would be used. In any case the payment of the total amounts in the above table is expected. If the transport tax is applied to the payment of the 1925 annuity, then the German Government could recover a similar amount out of the preferred railway stock when sold. Or the 1925 payment might be two hundred fifty million marks from transport tax, two hundred fifty million from sale of preferred stock instead of five hundred million from sale of preferred stock.

The payment of these amounts in the early years is insured, first, by holding the demands well within the amounts which a theoretical consideration of the budget indicates as being payable, and, second, by using five hundred million marks of outside money from the sale of railway preferred stock, eight hundred million marks from a foreign loan, reserving for use if necessary about five hundred million marks from the transport tax.

But even if the consideration of these figures demonstrates the possibility of raising these amounts, it is hardly to be supposed that creditors would accept the mere promise of the present German Government to make a sincere effort to have

its people sustain the taxes necessary to carry it into execution. The offering of tangible guarantees is necessary to give assurance to all nations that the necessary taxes will actually be collected. Such guarantees will also relieve the German people of the political controversies certain to be engendered if the continuation of payments were dependent entirely on the popular will. In establishing such guarantees, every precaution has been taken to avoid any unnecessary interference with the actual control by the German Government over its revenues and expenditures.

The proposal is that certain revenues—those derived from customs, alcohol, tobacco, sugar and beer—should be assigned to, and be under the control of, Germany's creditors; that the taxes collected from these sources should pass directly into the hands of this controlling agency; that the payments due to creditors should be made from such funds and the balance given to Germany for its own purposes. The estimated yield from these sources for the year 1928 is about two billion marks, exclusive of customs, and there is every assurance that these assigned and controlled revenues will give a large margin over the requirements for payments from the budget, which at that time will be one billion two hundred and fifty million gold marks. These revenues supply a security that the specified payments will be made. There will be no inducement for the German Government to check the payment of such taxes, for the lack of revenue from this source would not excuse her from the repara-

tion demands, and any excess of taxation income from this source over such demands would be returned to it. The German Government could not reduce the rate of the assigned revenues without the consent of the Commissioner of Controlled Revenues, who shall be appointed by the Reparation Commission to take charge of these taxes. Such a Commissioner should be given adequate powers to supervise the collection of these taxes, and the plan is that he should have five subcommissioners, one for each of the controlled revenues. It would be the duty of this Commissioner to see that the administration was efficient and the accounting system correct, but he would not be expected to interfere with the administration of the law by German officials, except in the case of maladministration, and in no case would there be any interference in the tariff policy of the German Government.

An additional precaution to protect Germany against the danger of deficiency of budgetary income is afforded by specifying that if the yield of these controlled revenues falls short of one billion marks in 1926, or one and one-fourth billion marks in 1927, the reparation payments will be diminished by an amount equal to one-third of such deficiency, and on the other hand, if they exceed these limits, there will be an additional payment equal to one-third of the excess, but the deduction or the addition shall in no case exceed two hundred fifty million marks in each year. This system of control is more fully explained on pages 391-395.

In this chapter there have been outlined the payments to be demanded from Germany and the agencies which insure to the creditor nations the performance by Germany of the terms of its contract. The responsibility of converting these payments made from the proceeds of taxation and from the earnings of specified properties into credits outside of Germany is not placed on the German Government. When the payments that have been described in this chapter are made in the bank of Germany to the credit of the Allied Nations, the contract that is outlined in the plan of the Committee has been complied with. The German Government has no further obligations.

CHAPTER VII

STATUS OF REPARATION PROBLEM AT THE TIME OF COMMITTEE'S MEETING—THE NEW METHOD OF APPROACH—RESPONSIBILITY FOR CONVERSION OF INTERIOR PAYMENTS INTO PAYMENTS ABROAD ASSUMED BY GERMANY'S CREDITORS—WORK OF EXPERTS—RESTORATION OF CONFIDENCE NECESSARY—COMPLETION OF BANK PLAN—THE TRANSFER COMMITTEE—THE AGENT GENERAL—THE COORDINATION OF CONTROLS—OPENING OF WORLD'S CREDIT TO GERMANY—SALE OF GERMAN SECURITIES TO RESTORE WORKING CAPITAL—PLAN COMPLETED IN THREE MONTHS—UNANIMITY OF ITS MEMBERS—FINAL SOLUTION FOR FUTURE DETERMINATION.

The definite burden which had been laid upon Germany by the action of the Reparation Commission was for the payment of two billion marks annually, plus 26% of the value of its exported goods. The bonds which were issued in connection with these charges were not the measure of the indemnity fixed, but the circumstances of their isssue left the impression, throughout the world, that an indemnity of one hundred thirty-two billion marks was laid as a definite obligation upon Germany, which it was the intention of the Allied Powers to collect. This impression might easily have been corrected by a study of the proceedings at the Versailles Con-

ference, and at the various meetings of the Reparation Commission. But to have corrected the misapprehension would not apparently have produced favorable political results in any of the great nations, and therefore the impression deepened into conviction, which became the basis of all arguments that the indemnity was one hundred thirty-two billion marks, and that this was beyond the capacity of Germany to pay.

Under these circumstances it was urged, with almost universal approval, that the first step toward a settlement ought to be to measure the capacity of Germany to make payments, and then to fix the limit of the demands within that capacity. This capacity was obviously to be measured over a long period of years by the surplus of goods which Germany could export in excess of those which she required for subsistance and the maintenance of production. The attempts that were made to determine what this surplus might be brought forth figures from various eminent economists, in which all agreed to this extent, that it indicated the returns to be expected would be much below what the creditor nations had anticipated, and of which they stood in great need. If the total demands to be made upon Germany were limited to the sums that were to be fixed by economists after a study of that country under existing conditions, then it would happen both that the creditor nations would be disappointed in their expectations and that the people of Germany would carry a burden of indebtedness much less than the burden that was being carried by all of

those nations which would be her future industrial competitors. The contemplation of such a settlement was offensive, both to the universal sense of justice and to the sense of security in the field of industrial competition. Demands had been made upon France to reduce her claims below the minimum of twenty-six billion marks out of the A and B bonds, and such additional amounts as might be necessary to cancel inter-allied indebtedness. But as France had already expended about the sum of twenty-six billion marks in uncompleted reconstruction and as her people were expecting reimbursement for these expenditures, the French Government did not feel that it could reduce its claim for reimbursement on this account, nor did she regard it as possible to relinquish a claim for further collections out of which to make payments to the United States and to England. Her obligation to these countries amounted to a sum that would be the equivalent of about thirty billion marks. With a population of forty million as compared to a population of sixty million in Germany, this indebtedness alone constituted a weight upon France about equal to an indebtedness of Germany of about forty-five billion marks. The relinquishment of a claim by France for some additional reimbursement might have looked like a repudiation of its obligation, or, at least, like the exercise of liberality at the expense of her creditors. The continued pressure upon France to make further concessions created irritation and resentment within that country.

As has been stated before, it is not probable that

the Committee could have made much progress had it pursued the effort to make a settlement along such lines. Although it must have been recognized by all of the members that the element of novelty in the treatment of this problem would be, in itself, an advantage, it was rather the conviction that justice required it, that moved them to adopt the course which at the very first conference was outlined. This course was to consider that the problem of fixing the payments to be made by Germany and to be delivered to its creditors, was a double problem, one involving the burden to be assumed by Germany and the other the manner of delivering the benefits to be received by the creditor nations. In considering the burden to be laid on Germany, it seemed both fair from the standpoint of justice, and necessary from the standpoint of creating equality in the industrial conditions of all competing nations, that a burden of taxation should be laid on Germany which should be approximately equal to that which must be borne by its creditors and competitors. And having reached this conclusion the Committee faced an entirely different, although related, question as to whether and to what extent the proceeds of such taxation could be converted into foreign credits, and thus paid upon the reparation account.

In all their subsequent discussions, they divided the consideration of these questions, and in their final report, as explained in the preceding chapters, they outlined certain minimum requirements that must be met by the German people in providing the money that shall be available for payment to its

creditors. When the German Government has complied with this obligation, it will have fulfilled the contract which the Plan of the Committee would embody. The responsibility for converting this accumulation of payments within Germany into such form as would be acceptable to its creditors is assumed by the Allied Powers. The system of control consisting of Commissioners to supervise the operation of railways, the organization of mortgages and the collection of taxes, is the method by which the performance by Germany of the terms of its contract is guaranteed, and with the exception of this supervision, the outside governments will have no further responsibility in connection with the raising of the funds within Germany.

The very idea which at our earliest meeting was expressed and emphasized by Mr. Young was never out of the minds of the members of the Committee in all of their meetings—that it was necessary, first, to establish confidence throughout the world in the certainty of the reconstruction of Germany, and at the same time to inspire in the German people, themselves, such hope for the future as to call forth their greatest energy. Under the first part of the Committee's plan, the payments to be demanded of Germany upon its obligations are to be made within Germany and in German money. These payments having been thus made, the obligation of Germany is discharged. Had the obligation been placed on Germany to make such payments to its creditors outside of Germany, no matter how great the difficulties, then it is doubtful if the confidence

of the world could ever have been established in the stability of the German currency, in the ability of the German Government to balance its budget, or in the restoration of the productive power of the German people. And just as precautions were taken to guard against excessive demands in fixing the amounts which were required from Germany to be paid within that country, so the Committee has exercised care in fixing the conditions by which this accumulated fund could be paid to German creditors without destroying the power of that country to make further payments. Nothing is to be asked from Germany that she can not or ought not to pay, and nothing is withheld from its creditors which under any circumstances could be collected.

The Committee has in a general way considered this problem as an adjustment between debtor and creditor, with due regard to the future business relations between them, and in making its adjustments has realized that the interests of the creditors require that the credit of the debtor should be protected, and his productive power sustained. The previous treatment of the problem had necessarily sprung out of the conditions of war, and the Treaty of settlement. This Treaty was a settlement dictated by victorious nations upon a conquered people, and this relationship, in spite of efforts to avoid it, interfered with the unrestricted application of economic law and business principles in making the adjustments. By dividing the question into these two component parts, there was accomplished a satisfaction of war-engendered feeling by the an-

nouncement, as a moral principle, that commensurate burdens should be laid upon the people of all nations, as a consequence of war and not of defeat in the war, and at the same time an opportunity to avoid the disputes as to the economic effects of making an excessive demand by submitting this matter to the test of experience under an adjustment by which from year to year only such payments would be demanded as could be made without injurious effect.

The calling of these Committees of Experts was a direct result of the address made by Secretary Hughes at New Haven in December, 1922. Nearly a year elapsed before a formula could be found that would satisfy all of the governments. As has been stated, Secretary Hughes expressed to the members of the Committee the very strong confidence that their work would be successful. Both in his speech and in his talk with the members of this Committee before they left for France, Secretary Hughes laid emphasis upon two ideas, and although they seemed simple, over and over again the importance of them was impressed upon, at least, the American members of the Committee. These ideas were that a settlement must lay the foundation for confidence in the future of Germany, and restore conditions of productivity within that country.

To carry out this plan required the gathering, digesting and interpreting of a great mass of material already collected by the Committee of Guaranties, and of additional information affecting the particular aspects of the problem to be

considered. The staff of experts assigned to the American members were given this great task, and in addition were called upon to submit opinions upon all of the principles that would be involved in making these adjustments. A similar staff of expert economists and investigators was attached to the Committee members from other nations.

Upon the shoulders of these men whose names are well known in connection with other important accomplishments, the great volume of this work was laid, and without there being any prospect that they will receive the credit and recognition which is rightfully theirs, for such merit as there may be in the finished plan of the Committee. It was gratifying to observe that the papers prepared and the opinions expressed by the members of the American staff received most respectful consideration by the other members, as well as by the American members of the Committee. But while the American members of the Committee, at least, relied upon the knowledge and were guided by the opinion of these expert advisers, it is not to be assumed that any one of them is responsible for, or has endorsed in detail all of the conclusions that are embodied in the report, itself.

There were conflicting opinions which required adjustments, and for the compromises which necessarily were made in order to bring about an agreement, these expert advisers are not responsible. But should the plan of the Committee meet with the acclaim of the world, then to the names of Dawes and Young and Robinson will be added credit and re-

nown for performances for which a large part of the credit ought to go to such men as Kemmerer, Davis, Goldsmith, Ayres, Tower, Herring and Jones. And when many of the circumstances which attended the various conferences are recalled, it is not to be doubted that General Dawes and Mr. Young and Mr. Robinson would wish to express the very greatest obligation for the assistance that was rendered by Colonel James A. Logan, Unofficial Observer for the United States at the Reparation Commission. His knowledge of the entire situation and his great ability and good judgment were always at their service and at all times during the conference they were in close consultation with him, and greatly influenced by his advice.

The discussion by Doctor Kemmerer, which was included in Chapter Four will give a suggestion of the strong automatic forces tending toward the equilibrium of currencies in international trade, and should be reread by those who wish to understand the full effect of the precautions taken in organizing a plan for the transfer of credits out of Germany. It is probable that the realization of the disastrous consequences which might result from overstraining the resources of Germany by the transfer of such large credits, has led to an exaggeration of the danger of such a condition being produced. The multiplying of precautions against such a disaster will certainly have an effect of strengthening the confidence of the world in the soundness of the plan and in the security of the bank and in general business conditions in Germany.

With the establishment of complete confidence, it is pertinent to remark that the new bank would have very soon after its organization not only the entire amount of the capital stock, four hundred million marks, but, as pointed out in the last chapter, would be strengthened by the use of eight hundred million marks from the foreign loan, and the report of the Second Committee indicated there was more than a billion marks of foreign currencies in hiding within Germany, and nearly six billion marks of foreign credits held by Germans in banks throughout the world, or in credits much of which could be transferred into bank balances. The greater part of this would necessarily come into circulation and active use as soon as the complete confidence of the world was established in the soundness of the new bank. It was, however, realized by every one that all those restrictions must be thrown about the bank, which would be necessary in order to assure the world that it stood upon a sound foundation, and would operate under such restrictions as to give assurance of the stability of its currency.

But before discussing in detail the plan that was finally adopted for the organization of the bank, it may be well to mention other strong automatic forces that would operate toward an equilibrium of the currency values of the world, aside from the ones connected with the operation of banks. These are the effects produced on industrial activity by the restoration of confidence and the inspiration of hope among the people, and the resulting increase in their productive power. The greatest burden

that was laid on labor in Germany was the uncertainty of its reward. As soon as the German laborer knows that the mark he receives for a day's work will have an unchanging purchasing power, he will be relieved of what has been his greatest anxiety. And when the managers of German enterprise are freed from the uncertainty that is created by a lack of confidence, their enterprise and activity will be reawakened. The productive power of Germany will be stimulated. The development of this productive power will both increase the capacity of the nation to pay taxes in German money, and increase the exportable surplus of goods, which, in turn, will provide the credit through which payments may be made in foreign currencies or credits. At the same time there will be, for a period at least, as a direct result of higher taxes, a certain reduction in the purchasing power of the German people, and this will tend not only to the restriction of imports, but to the exercise of wealth-producing thrift. Upon such a scale as is now under consideration, it is probable that the payment of such increase in taxation will register itself in an almost corresponding increase in exports. The underlying presumption is that confidence will be restored and production upon a large scale reestablished. Should production be reestablished on a large scale, then in view of the forces set in operation as explained by Mr. Kemmerer, there will be practically no danger of calamity, or even difficulty in making foreign payments at the time and in the amounts as a surplus accrues from the new scale of taxation.

Mr. Kemmerer's argument was made upon the assumption that the new bank would be a gold bank, and under ordinary circumstances there would be no dissent. But such has been the disturbance in international trade in recent years that the old conditions of exchangeability of the various currencies upon the gold-standard basis have not been maintained. Strictly speaking, none of the great banks of Europe is to-day upon a gold-standard basis. It was the impression of the experts connected with the American Committee, at least, that to establish the new German bank upon a strict gold basis would help the other banks to restore the same conditions. But there was a great opposition from those who seemed to be in a position to test the sentiment prevailing in the banking circles of Europe. It is difficult to determine whether this opposition sprang from a fear that the establishment of such a standard for the German bank would force the other European banks to a premature acceptance of the same conditions, or purely out of a kind of jealous resentment, that a better banking system should be established for Germany than existed for any other great nation of Europe.

At any rate many suggestions were made of modifications of the standard for exchangeability, and especially of the character of assets which might be held in the reserves against which currency was to be issued, some of which received great support, both in and out of the Committee, and all of which seemed, from the standpoint of the American experts, to be of such a nature as to leave a dangerous

freedom to those who were to be in control of the bank.

The bank plan as finally adopted will be found in Annex No. 1. Sections 12 and 13 are those which prescribe the conditions controlling the reserves and the issuance of bank-notes. The modifications from the original proposals for a bank upon a strictly gold exchange basis are found in these words:

"The Committee is of the opinion, however, that at the inception of the bank, conditions will be unfavorable for the application of the above rule of convertibility; in this event this rule may be temporarily modified by the affirmative vote of every member but one of each of the following groups, the Organizing Committee, the Managing Board and the General Board. In case of such modification, the bank shall make all possible efforts and use all the means at its disposal in order to maintain the rate of exchange of the mark at as near gold parity as possible. Furthermore, in case of modification of the above mentioned rule of convertibility of notes, a return to convertibility will be permanently established as soon as possible, by a simple majority vote of the General Board, and of the Managing Board."

That is to say that the rules laid down for the convertibility of notes upon a gold-exchange basis shall be enforced, unless at the outset all of the members, except one of the Organization Committee (which is composed of one member of the Committee of Experts and the present President of the

Reichsbank), and every member but one of the Managing Board (which will be composed of Germans connected actively with the operation of the bank), and all of the members, with the exception of one, of the General Board (consisting of fourteen members, of which seven are Germans, and one is from each of the following nationalities, British, French, Italian, Belgian, American, Dutch and Swiss), are of the opinion that the rule ought to be modified.

In other words, there must be practical unanimity from the standpoint of German interests and from the standpoint of Allied interest, that a deviation from this strict rule is necessary for the stability of the bank and the security of German business. Should there be but two members of the Managing Board, who would object to the suspension of this rule, it could not be suspended, and should there be but two among the seven representatives of foreign nations who had objections, then the rule, as set forth in the plan, would be enforced. But if in response to the practically unanimous opinion of those actually charged with the responsibility of managing the bank, whether Germans or foreigners, it becomes necessary to suspend, for the time being, this rule of convertibility, then the rule may at any time thereafter be restored by a mere majority vote, and having once been restored, it can not thereafter be altered.

This proposal could not be rejected. Upon the other hand it was probably accepted by all of the members of the Committee as being an improvement

over the original suggestion, in that it provided a certain flexibility, which would enable those in control of the bank to make adjustments for its security. To be denied any freedom whatever in the matter, and to be held rigidly to a specified course of action might have created a situation in which even the unanimous judgment of all of the Directors and Managers of the bank could not avert disaster. In such a case it is more likely that a conference of Premiers with the German Government would have resulted in such adjustments being made as have in the other great banks of Europe been made in order to avoid inevitable disaster.

The difficulties that were apprehended in connection with this transfer of money seemed upon closer study to grow less rather than greater, but the knowledge of the universal fear of an injury which might be created by too hasty withdrawals has led the Committee to adopt every precaution, which could be suggested to avoid it. The greatest reliance is placed upon those automatic operations of the law of supply and demand, which were so clearly described in Mr. Kemmerer's paper. There is not much danger under the circumstances, and this release from the inflexible rule of convertibility by the unanimous action of these respective bodies in control of the bank, gives them necessary freedom of action to adopt the usual remedies, in case of the appearance of danger universally recognized.

But nevertheless, and perhaps chiefly in order that the confidence of the banking world might be estab-

lished in the permanence and security of this new bank, there has been provided by the Committee a special plan and method of bringing about the transfer of reparation payments from German currency into foreign currency, together with suggestions as to the use that may be made within Germany of such balances as are not for the moment transferable. And in general these plans provide that the transfers of funds shall be made to the extent which in the judgment of the Committee the foreign exchange market will permit, without threatening the stability of the German currency; and having laid down this rule, authority is given to those in charge of the transfer of payments to make investments in German bonds or securities. When the accumulation of funds not transferable shall have reached the sum of five billion marks the payment for Treaty charges shall be reduced to such an amount as is susceptible of transfer and the Committee by a two-thirds vote shall have the power to suspend the accumulation, even before reaching the five billion marks.

The text of these provisions is here reproduced in order that the reader may have complete knowledge of the protection provided in the plan of the Committee:

THE TRANSFER
OF REPARATION PAYMENTS
FROM GERMAN CURRENCY IN-
TO FOREIGN CURRENCY AND
THE USE OF BALANCES NOT TRANSFERRED

TRANSFER COMMITTEE

1. The plan provides that all payments for the account of reparations, however derived, are to be first made in the form of deposits in the bank, provided for in the plan, to the credit of 'The Agent for Reparation Payments.' The withdrawals from this deposit shall be made by the Agent for Reparation Payments only, under the direction of a Committee composed of five members known as "The Transfer Committee."

COMPOSITION AND SELECTION OF MEMBERS

II. The Transfer Committee shall be composed of six members; the Agent for Reparation Payments shall be a member and the Chairman; the other five members shall be persons qualified to deal with foreign exchange questions. They shall consist of an American member, a French member, an English member, an Italian member and a Belgian member. Each of them shall be appointed by the Reparation Commission, after the member of the General Board of the Bank of the same nationality has been consulted.

COOPERATION OF THE BANK

III. The Committee will be in contact with the President and the Commissioner of the Bank.

POWERS OF THE COMMITTEE

IV. The Committee shall have power, and it shall be its duty:

a. to apply such bank balances for payments

for deliveries in kind and payments under the Reparation Recovery Act, in accordance with the program established periodically by the Reparation Commission, after consultation with the Transfer Committee as to the character and amount of such deliveries;

b. to convert these bank balances into foreign currencies from time to time and, after conversion, to remit them in accordance with the instructions of the Reparation Commission.

Both the foregoing powers (a) and (b) to be exercised to the extent to which in the judgment of the Committee, the foreign exchange market will permit, without threatening the stability of the German currency.

c. to invest from time to time in bonds or other loans in Germany, such amounts as the Committee may deem wise. The Committee shall proceed to make these investments as soon as the amount of the credits exceeds the sum which the Bank will keep on deposit. On the other hand, the Committee may sell the bonds which it has acquired, or liquidate the loans which it has granted, whenever in its opinion the sums may be converted into foreign exchange, or the Bank can accept additional deposits.

RESTRICTION ON PURCHASE BY THE CREDITORS

V. The goods supplied by Germany to the creditor countries under Paragraph IV above and paid for by the Bank as above provided, shall be for the sole use of the countries receiving them for

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United States Member Second Committee of Experts

their internal requirements, including the requirements of their colonies and dependencies. The goods so delivered shall not be exported from the country receiving them, except by agreement between the Committee acting unanimously and the German Government.

VI. In addition to its powers under Paragraph IV, the Committee may on the instructions of the Reparation Commission and at the request of the Creditor States, by debiting their accounts, transfer marks to private individuals for the purpose of making purchases in Germany, such reinvestment not to be of a temporary character, and such property being of classes contained in a schedule agreed to between the Committee and the German Government, and modified from time to time by similar agreement. In arriving at such agreement, the German Government shall be required to have due regard to the necessity for making maximum payments to its creditors, but it shall also be entitled to have regard to maintaining its control of its own internal economy.

COOPERATION BY THE GERMAN GOVERNMENT AND THE BANK

VII. The German Government and the Bank shall undertake to facilitate in every reasonable way within their power the work of the Committee in making transfers of funds, including such steps as will aid in the control of foreign exchange. When the Committee is of the opinion that the Bank's discount rate is not in relation to the necessity of mak-

ing important transfers, it shall inform the President of the Bank.

ATTEMPTS TO DEFEAT TRANSFER

VIII. In the event of concerted financial maneuvers either by the government or by any group, for the purpose of preventing such transfers, the Committee may take such action as may be necessary to defeat such maneuvers; and in such circumstances it may suspend the operation of Paragraph X, may accumulate the funds or employ them in the purchase of any kind of property in Germany.

TAX EXEMPTION PROVISION

IX. The German Government shall not tax the deposits in the Bank or goods purchased for the creditor countries pending removal, nor any securities or loans representing investment of funds pending transfer, nor any property purchased under the provisions of the paragraph next preceding. This exemption does not apply to property purchased under Paragraph VI, but on the other hand, there should be no tax discrimination against such property.

PROVISIONS FOR LIMITATION OF ACCUMULATION

X. a. When the accumulation of funds not transferable under the provisions of subdivisions b and c of Paragraph IV shall have reached the sum of five (5) milliard gold marks (whether represented by bank deposits or loans), the payments for Treaty charges provided for shall be reduced to

such an amount as will cover the transfers and payments provided for under subdivisions b and c of Paragraph IV without additional accumulation. Such partial suspense of Germany's obligations shall be operative only during the period that the conditions of transfer necessitate, and the standards of payment laid down in the plan shall be resumed at any time when they can operate without the limits of accumulation herein laid down being exceeded.

b. The Committee shall have the power to suspend accumulation before reaching five (5) milliard gold marks, if two-thirds (2/3) of its members are of the opinion that such accumulation is a menace to the fiscal or economic situation or to the interests of the creditor countries.

c. The Committee shall, by a two-thirds (2/3) majority, have power to waive the limit accumulations under the conditions provided for in Paragraph VIII.

The Agent General is here recognized as the Chief of the organization created. He receives all payments for the account of reparations, deposits them in the bank, and withdraws such deposits under the direction of the Transfer Committee, of which he is Chairman, to pay for deliveries in kind or to invest in bonds or other loans in Germany, and has power to sell the bonds acquired and collect the loans and to pay the balances to the creditors of

Germany. In commenting upon the functions of the Transfer Committee the Report states:—

"They will control the transfer of cash to the Allies by purchase of foreign exchange and generally so act as to secure the maximum of transfers without bringing about instability of the currency. We do not deny that this part of our proposal will present difficulties of a novel character which can only be solved by experience. But what are the alternatives? In order that no difficulties with exchange or stability can possibly arise, the sum payable for reparations may be definitely fixed at such a figure as is certain beyond all doubt to be within Germany's capacity to export in excess of her imports. In this case the attainment of such certainty would involve so low a figure as to be quite unacceptable to her creditors and unwarrantably favorable to Germany. On the other hand the liability may be fixed without regard to that excess of exports at all, and the discharge of the liability left to uncontrolled events without any possible regard to exchange difficulties. That way lies future instability and disaster. We are convinced that some kind of coordinated policy with continuous expert administration in regard to the exchange, lies at the root of the reparation problem and is essential to any practicable scheme in obtaining the maximum sums from Germany for the benefit of the Allies."

It will be seen that the control of these payments in foreign exchange will always be in the hands of experts in foreign exchange, and men well trained in the science of banking under instructions to limit the transfers in such a manner as to protect the stability of the currency and the solvency of the central bank.

In addition to the duties of the Agent General as

outlined above, he is designated as the coordinating agent between the Reparation Commission and the various Commissioners. "The Commissioners would retain all responsibility for the carrying out of the task entrusted to each, only subject to such coordinating policies as may prove necessary in order to avoid any duplication of effort, overlapping of functions, unnecessary friction and generally all interference with the harmonious working of the plan.

"In case of a difference of opinion between one Commission and the Agent General for Reparation Payments in his capacity as coordinator, the Commissioner can appeal to the Reparation Commission. The existence of this right of appeal will have a salutary effect upon the relations of the Coordinating Agency and the different Commissioners.

"To facilitate the interchange of information which will develop a situation in its entirety for appropriate action, a general Coordinating Board is also suggested in which the various Commissioners or representatives named by them will participate together with the Agent General for Reparation Payments and the Trustee. The Coordinating Board is to have advisory powers only and is for the purpose of giving information to the Agent General to assist him in preparing coordinating orders."

The Agent for Reparation Payments in his capacity of receiving the funds, and as Chairman of the Transfer Committee in disbursing them and as Chairman of the Coordinating Board (from which he may receive information and advice) will be an official of great power and dignity, upon whose in-

itiative, wisdom and discretion the success of the scheme will quite largely depend.

The economic consequences of inflation in Germany, those to be expected immediately and those to follow after in later years, are as pervasive in the whole problem as they are elusive. They affect the study of the problem of transferring funds and credits out of Germany in a very important manner. The following sentences are taken from the Report:

"The extinction of the German debt has after all been at the expense of her own Nationals who are her taxpayers. . . . The loss incurred by individual holders of debt is exactly offset by a corresponding profit to the taxpayers as a whole." But in this process certain classes benefited and others were despoiled. If nearly twenty billion marks of savings-bank deposits were wiped out and if the total bank deposits in January, 1924, were only one-seventh of those existing in 1914, then there must be accumulated at least forty billion marks of capital more than is now in use before a normal condition of working capital and credit can be reestablished. If there be doubt as to Germany's ability to establish such conditions as to make exterior payments possible, certainly it will be a difficult matter both to accomplish that and accumulate this lost working capital.

The Committee was not foolish enough to open such intricate and controversial subjects as the amount which has actually been paid for reparations. Much has been paid, and some that has not produced an economic benefit in the receiving

countries of an equal weight to the loss sustained by Germany in making the payments. But among Germans the idea persists that the actual payment already made through reparation is about equal in value to the loss of its working capital as represented in bank deposits. They believe this must be restored before normal conditions may be considered as being reestablished. This would explain why they look so anxiously to the opening of credits for their industry especially, and from America in particular. They accept the plan, and chiefly for the reason that it appears likely from their point of view to reestablish mutual good will and provide the basis for credit.

They do not believe that all international trade ceases, when, for a period, exports are less than imports; under such circumstances trade continues in response to the necessities of the case, and the balance is taken care of, first out of invisible exports, that is interest on foreign investments and services of various kinds, and secondly and chiefly by a shifting of credits and investments. And it is from this shifting of credits and sale of securities that they anticipate the earliest and most beneficial effects from the substitution of this plan for the continued control by the Reparation Commission, for after all this is the alternative; the old control or the new one must prevail from now on in the handling of the reparation problem.

The Germans with their fixed capital freed from all indebtedness through inflation, hope under the new plan to be able to borrow enough to restore

their working capital lost through the same process; and the sums required for this purpose, though large, are much smaller than would have been required if it had been their fixed capital which was destroyed. With their capital thus restored, they will work under the most favorable conditions to establish that ultimate surplus of exports upon which their solvency will depend.

Enough has been said in the course of these comments to indicate the confusion and the controversies created by the handling of the matter of reparation under the Treaty of Versailles. The reparation problem was only one of the many adjustments made under that historical document: boundaries were fixed, new governments created, a league of nations established, and mutual obligations formed between the contracting nations.

The arrangement for the distribution of authority among the various bodies of control established probably followed the precedents of other Treaties. The source of authority was the Treaty and the authority was granted by the governments. The Reparation Commission and all the other bodies of control were the creatures of governments. It would be idle to find fault with this arrangement as being a political control. The governments were obliged to act in their sovereign capacities and necessarily under political restrictions. The day is past when any part of such international agreements can be made in secret. Every part of them is open to the world and may arouse the fear and jealousy or excite the hopes of masses of people. When all governments

are more or less democratical, such matters, being of great importance to the general welfare, become matters of general discussion. The relations between governments and the cooperation of governments under Treaties for the accomplishment of their common purposes, are political in their nature and must be placed under political control.

But when economic interests of great importance are placed under political control, there is necessarily produced confusion, duplication of effort and delay. In making political changes, delay may be considered salutary, but its effect upon economic processes is destructive and intolerable. The important subject of reparations was one of great economic importance. The matter of dealing with it under organizations necessarily of a political nature had produced conditions almost unendurable and threatened the world with a new disaster almost as serious as that from which it was just then emerging. The people of Germany, prostrated by the effects of inflation, found their industrial regions under the control of outsiders, custom barriers erected within their own country, their railroad system divided and disorganized and until they could gather their strength and resume the use of all their own resources they could not hope to be able to meet the demands of their creditors, nor even to maintain the momentary stability of their curious currency. They tottered on the verge of another and more terrible collapse. The effects of such a disaster in Germany would be felt by all the nations, but even before sustaining them, these other nations would

soon have had a serious crisis to meet in the growing distrust and resentful jealousy springing up between themselves.

It is perhaps as unprofitable to discuss what might have been as to speculate about what might hereafter be. But nowhere has there been heard, either in France or Germany, any dissent from the opinion so often expressed that a great disaster was impending over Europe at the moment when the Committees of Experts was called into existence. This condition must be remembered in judging of the work produced by these men. Any adjustment will be a good one which averts the immediate disaster. In no other manner than through the action of this Committee to be endorsed by the Reparation Commission and ratified by the contracting governments can the Treaty of Versailles be rewritten. And by this process it can be rewritten in certain particulars only. The Report of the Committee is a revisal of certain portions of the Versailles Treaty, not a new adjustment outside of the Treaty. It was limited to the scope of its inquiry, not only by Section 134 to which reference has already been made, but by all the conditions, political and economic, which have grown up as a result of the war. Let no man criticize it, therefore, as if it had been prepared for a world unscarred by war, and by men entirely free to work out at their leisure, novel and scientific remedies for a hypothetical disease. In less than three months the work of these Committees was completed, and every day of delay for its final presentation was a source of anxiety to the members.

Working under such limitations and under such pressure it is not to be doubted that some errors and omissions have marred their work.

But in general they have outlined a plan which attempts to separate the political portions of the Treaty from the economic ones and to place the economic matters under a business control to the extent that it is possible to create such a control over adjustments in which the important interests of government are concerned.

The acceptance of this report by the Reparation Commission may be taken as evidence of a sincere desire on its part to avoid a great disaster, for it will be in effect an act of abdication of its powers. The greater part of the authority and responsibility for handling these important matters will be assumed by the Agent General and the various Commissioners. The Reparation Commission will have as its most important function the appointment of the various Agents and Commissioners who will conduct, under business rules, the great work of collecting reparations formerly entrusted to the Commission itself.

The system outlined results in the minimum of interference with the German administration and avoids so far as possible interference by all other governments in the agencies it creates. The Banking System of Germany is reorganized and committed to the management of Germans; its railroad system mortgaged for Germany's creditors and managed by German nationals; its special revenues assigned as security but without interference in

their collections; and all exterior payments limited in such a manner as to insure against injury by excessive payment under the control of an organization so far removed from political influences as any body of men in the world could be.

But the plan in the nature of things could not have cancelled indemnities nor extinguished international indebtedness. It could not have rescinded the Treaty nor effaced the hardships which come as the aftermath of war. At first it will be hailed with relief, accepted with enthusiasm, and if so Germany's credit will be reestablished, its industrial machinery set to work. Thereafter complaints will come, from the Germans, first, perhaps, that the control of railroad freight rates by outsiders is an impossible burden, and that no government ever ought to have given up a control over an agency which in regulating freight rates could both minister to justice as between its own citizens and add to the national power in international competition by discriminatory treatment of exporters. And when the bank credits are restricted, it will be attributed to the foreign supervision over the bank. And in other parts of the world, as Germany gains in industrial power, and the competition becomes severe, there will arise the cry that the application of this plan has increased the German production to such a point as to remove opportunity from the workers of other nations, and that the effect of collections of international debt is to lay a burden upon the laboring men of all countries in order that the holders of the bonds of the respective nations of the world may continue to collect their interest.

If the plan is put into operation, even though the immediate relief is felt as being salvation from great disasters, the day may come when it will be held responsible for all the hardships which must be endured in the future. The very existence of indemnities and international obligations condemns the world to serious strains which the most perfect machinery could only relieve, but not remove. The scars of war are not to be healed without suffering. In the future there will be many who will say that it is the plan and not the Treaty, the mistakes made since the war and not the war, that have caused the difficulties which are likely to present themselves. But the unanimity of this Committee is the sign of a better spirit, upon the further development of which the peace and prosperity of the world depends. In the operation of the plan there must always be applied that same spirit of Christian forbearance to which Chancellor Marx appealed when it was being formulated.

THE END

APPENDICES

No. 1. The Evolution of the Terms of Reference to the Committees of Experts

No. 2. Resolutions Adopted by the Reparation Commission on November 30, 1923

No. 3. Report of Committees of Experts to Reparation Commission: Complete English Text with Annexes

APPENDIX NO. 1

THE EVOLUTION OF THE TERMS OF REFERENCE TO THE COMMITTEES OF EXPERTS

On November 30, 1923, the Reparation Commission decided to create two Committees of Experts, pursuant to the authority vested in the commission by paragraph 7 of Annex II of Part VIII of the Treaty of Versailles, which reads in the pertinent part:

"The Commission is authorized to appoint all necessary officers . . who may be required for the execution of its functions . . to constitute committees whose members need not necessarily be members of the Commission . . and to delegate authority and discretion to officers, agents and committees."

The full text of the Commission's Decision, which indicates the motives which led to its adoption and which also defines the objects and scope of the two Committees' labors, is expressed in the English text in the following form:

"In order to consider, in accordance with the provisions of Article 234 of the Treaty of Versailles, the resources and capacity of Germany, and after giving her representatives a just opportunity to be heard, the Reparation Commission decided to create two Committees of Experts belonging to the Allied and Associated countries.

"One of these Committees would be entrusted with considering the means of balancing the Budget and the measures to be taken to stabilize the currency.

"The other would consider the means of estimating the amount of exported capital and of bringing it back into Germany."

The language just quoted should be read in the light of the contemporaneous correspondence relative to its meaning which was exchanged between M. Barthou, President, French Delegate to the Reparation Commission and Mr. Logan, U. S. Unofficial Observer at the Reparation Commission (Annex T). The British interpretation of the language is set forth in the letter of acceptance of Sir Robert Kindersley (Annex II). Article 234 of the Treaty of Versailles, in the execution and application of which, according to the Commission's Decision, the Committees are created, provides as follows:

"The Reparation Commission shall after May 1, 1921, from time to time, consider the resources and capacity of Germany, and, after giving her representatives a just opportunity to be heard, shall have discretion to extend the date, and to modify the form of payments, such as are to be provided for in accordance with Article 233; but not to cancel any part, except with the specific authority of the several Governments represented upon the Commission."

In appreciating the true scope of the present terms of reference to the Committee, it may be helpful briefly to state the three prior proposed formulas which were put forward, discussed and rejected—with some indication of the reasons for their failure of adoption.

FORMULA I

The present committee idea developed late in October, 1923, partly as the result of the almost simultaneous occurrence of three events. The Germans had asked for a hearing relative to Germany's financial situation and her ability

to pay reparations. Mr. Baldwin, to a degree stimulated by the Imperial Conference then held in London, was talking of a new international conference to discuss the whole reparation problem. President Coolidge had just stated publicly that his Administration still stood on Mr. Hughes' New Haven speech of December, 1922, which held out hopes of unofficial American expert participation. The coincidence of these public happenings, especially considering the existing impasse between France and England as to the proper reparation policy and the daily deterioration of Germany's finances, germinated the present committee idea and the idea became crystallized after England and France approached Mr. Hughes, through their representatives in Washington, and discovered that he was friendly to the creation of an expert committee providing it represented a genuine effort to accomplish something.

Formula I for submission to the Experts appears to have been fathered by M. Poincaré about October 26th. (It is to be remembered that the first negotiations concerning the committees and the terms of reference were carried on between the Governments. The negotiations which led up to the present Committees were carried on between the Reparation Commission and the Governments.) M. Poincaré's formula would have the committees study "the actual state of Germany's resources and capacity of payment." In French, actual (actuelle) means "present."

This limited formula found no favor either with England or with Mr. Hughes. M. Poincaré defended it legally on the ground that the language of the Treaty providing that the resources of Germany should be considered "from time to time" intimated that these considerations were to be frequent, periodic, and not once and for all time. He defended it practically on the ground that no one but a clairvoyant could forecast Germany's capacity to pay

twenty years hence. When pressed, he stated frankly that he did not wish the Committees even to consider the reduction or cancellation of any part of the German debt as fixed at 132 milliards. He advanced the legal argument that since the Commission was incompetent to reduce or cancel any part of the German debt, (only the Governments may do this—Article 234) consequently it was incompetent to appoint a committee which would consider, or recommend, such a step. He insisted that whatever committees were appointed should in no way usurp the powers of, or replace, the Reparation Commission and should in no way operate or recommend except pursuant to the terms and within the scope of the Treaty of Versailles. Although ready to assent to this last limitation neither England nor Mr. Hughes would accept the formula limiting the inquiry to the "present" capacity of Germany to pay; hence this formula was discarded.

FORMULA II

On November 7th the English, through Sir John Bradbury, offered an alternative and elastic formula proposing that committees should be created "with a view of examining the capacity of payment of Germany and of making proposals of a financial character likely to assure said payments." There were indications that Belgium and Italy would accept this language. France, through M. Barthou, immediately proposed an amendment in the following terms: "With a view of examining, *within the limits of the powers of the Reparation Commission,* the *present* capacity of payment of Germany and of making proposals of a financial character likely to assure said payments."

The French amendment, upon analysis, was really a repetition of M. Poincaré's first formula. The English proposal designedly opened the door to a discussion of the

entire reparation problem. M. Poincaré quickly indicated that so broad a reference was not acceptable to him. Lest an attempt be made to have the English text adopted by the Reparation Commission by majority vote, he called attention to paragraph 13 of Annex II of the Treaty, to the effect that questions involving the cancellation of the whole or any part of the debt or obligations of Germany required a unanimous vote, and he indicated that in his view the appointment of a committee with power to consider these questions would also require a unanimous vote. Since France was in opposition, the adoption of the elastic English formula could not, he suggested, be legally accomplished. In answer to Mr. Hughes' specific question as to what was meant by "present" capacity, M. Poincaré replied that the maximum period which could be considered should not extend beyond 1930. Mr. Hughes replied that under these considerations the United States could not participate even informally, and the three-cornered negotiations between France, England and the United States thereupon fell through.

FORMULA III

At the first meeting, (November 13th) of the Reparation Commission after the failure of the proposals above described, the Commission, acting in its own sovereign capacity, took up the Committee subject and the matter thereby entered into its second, and present, phase.

M. Barthou, the French Delegate, offered this text for consideration, explaining that it was preliminary in its character:

"This Committee should be charged with determining the capacity of payment of Germany at the present moment and to provide the Reparation Commission with the elements of a decision for fixing German payments during the three years 1924, 1925 and 1926. In the opinion of

the French Delegation these experts, who will take the Schedule of Payments as the basis of their work, should study the evaluation of the internal and external resources of Germany and particularly German assets abroad."

The proposal, upon scrutiny, proves to be even more restricted in its scope than any of its predecessors. M. Poincaré interpreted "present" to mean until 1930; formula III would stop at 1926. M. Poincaré was willing to permit the committees to operate within the scope of the Treaty of Versailles. Formula III suggested that they would operate within the limits of the Schedule of Payments—which was apparently an indirect method of indicating not only that they could not discuss any reduction of the debt fixed by the Schedule, but also that their sole aim and function was to discover ways and means of getting the Schedule of Payments carried out, i. e. the total paid. In this connection it is important to remember that the sum of 132 milliards was not fixed by the Treaty of Versailles and that the popular opinion that any discussion of the correctness or realizability of this sum amounts to a destruction of the Treaty of Versailles or an amendment thereof, is merely an illusion. Formula III, however, did contain an expression on a new subject—the matter of investigating German assets abroad.

Considering the fact that the previous and more liberal French proposals had not been acceptable, it was only natural that the tentative formula III, above quoted, should receive a luke-warm reception. The British Delegate referred to it as a prescription which belonged to a world in which a certain philosopher invented pills for the treatment of earthquakes. However, the proposal led to informal conferences between the individual Delegates outside formal sessions, and to unofficial conferences between them and Mr. Logan that finally resulted in shaping the present terms of reference which were introduced

by M. Barthou and which were unanimously approved by the Commission. Through Mr. Logan M. Barthou had first ascertained that the present formula (coupled with his letter of explanation) was sufficiently unrestricted in its mode of expression to enable Mr. Hughes to give his assurance that American experts would participate on such a basis. Indeed, there was some highly confidential intimation that the French would not obstruct a consideration of the whole reparation problem even including debt reduction, although if the report took any such form the French members of the Committee would doubtless dissociate themselves from that recommendation.

THE PRESENT FORMULA

"One of these Committees would be entrusted with considering the means of balancing the Budget and the measures to be taken to stabilize the currency.

"The other would consider the means of estimating the amount of exported capital and of bringing it back into Germany."

This language seems simple and free of legal subtleties or scholastic pit-falls. However, the letter of acceptance of Sir Robert Kindersley reflects a sensitiveness lest even this language be made the subject of controversy and discloses a desire to pin a definite and a broad interpretation upon it.

It would be a fault wholly to disengage the foregoing text from its context and to ignore the preamble of the Commission's decision in creating the Committees—"in order to consider, *in accordance with the provisions of Article 234 of the Treaty of Versailles,* the resources and capacity of Germany . . the Commission decided to create two Committees," etc. In other words, it appears that the Commission was acting by virtue and in application of its powers and duties under Article 234. It appears

logical that an advisory expert committee appointed by the Commission to aid in the execution of Article 234 should have no greater powers than the Commission itself under that Article. If any dispute as to the scope of the operations of the Committees arise, it is anticipated that arguments in restriction of their functions will be drawn from the assumed limitations of Article 234 rather than from the relatively clear wording of the paragraph describing the Committees' duties with reference to the German budget and currency. Article 234 is worth repeating:

"The Reparation Commission shall after May 1, 1921, from time to time, consider the resources and capacity of Germany, and, after giving her representatives a just opportunity to be heard, shall have discretion to extend the date, and to modify the form of payments, such as are to be provided for in accordance with Article 233; but not to cancel any part, except with the specific authority of the several Governments represented upon the Commission."

M. Poincaré's deduction that the expression "from time to time" limited the Commission to considering Germany's capacity for successive brief periods only has already been noted. This point may be raised again if and when it is suggested that intelligent and effective methods of balancing Germany's budget cannot be had without due consideration of the financial practicability of Germany's meeting and discharging *in toto* the biggest single obligation with which that budget is supposed to be charged.

The more likely objection is that inasmuch as by Article 234 the Reparation Commission cannot cancel any part of the German debt except with the specific authority of the several Governments, therefore its subsidiary committee cannot consider this question reserved to governmental action. The Paris Press has occasionally propagated this fallacy. Even if the Commission cannot itself,

without the consent of the Governments, cancel any part of the German debt, it can certainly discuss the question, investigate the question, and make recommendations to the Governments on the question, if, as the result of its investigating the resources of Germany it feels that such action is necessary or appropriate. That the Commission may consider the matter is conclusively proved by the language of sub-paragraph (f) of paragraph 12 of Annex II—"Decisions of the Commission relating to the total or partial cancellation of the capital or interest of any verified debt of Germany must be accompanied by a statement of its reasons." And again by paragraph 13 of Annex II to the effect that a unanimous vote of the Commission is necessary in questions involving "the cancellation of the whole or any part of the debt or obligations of Germany." Indeed, the very prohibition of Article 234 to the effect that the Commission may not cancel, without the authority of the several Governments, indicates with great clearness that it was foreseen that as a result of its investigations under Article 234 the Commission might be led to the belief that it was necessary to cancel a part of the German debt. To avoid this step without the consent of the Governments the prohibition quoted was inserted.

By a fair construction of Article 234, therefore, and of the present terms of reference, especially read in the light of the chronological development of the previous restricted formulæ and in the light of the correspondence between M. Barthou and Mr. Logan, it seems proper to conclude that the Committees are empowered to make all and every study and recommendations designed successfully to stabilize German currency or balance the German budget, quite irrespective of whether this study and these recommendations involve directly or indirectly some consideration of the global German reparation obligation.

It is highly to be hoped that none of these technicalities

will impede the free progress of the Committees' efforts—or even be mentioned. This memorandum has accomplished its full purpose by merely stating some of the legal aspects of a situation which, in practice, should be met or circumvented on common sense, business grounds, with a complete disregard of the legal niceties which, in the past, have so often become instruments of obstruction in dealing with the problems of the Treaty of Versailles.

L. F.

January 9, 1924.

CORRESPONDENCE BETWEEN M. BARTHOU, FRENCH DELEGATE, REPARATION COMMISSION, AND MR. LOGAN, UNOFFICIAL AMERICAN REPRESENTATIVE, REPARATION COMMISSION

M. Barthou to Mr. Logan:—

Délégation Française
à la
Commission des Réparations.

Paris, 5 December 1923.

My dear Mr. Logan:—

I have just had a conversation with our colleague, Monsieur Delacroix, upon the observations which you have exchanged with us. In order to give you more definite information, and to clear up points which might leave doubts in your mind, we desire to furnish you with more precise details.

The First Committee of Experts will endeavor to find:

(a) The means of balancing the budget,

(b) The measures to be taken to stabilize the currency.

Concerning the stabilization of the currency, the Experts would be invited first of all to determine the conditions to be realized in order that a currency may be stabilized, and then the measures to be progressively taken so as to realize all of these conditions.

As the stabilization of the currency necessitates budget equilibrium, the Experts would similarly be invited to study in detail the receipts and the expenditures of the Reich, and also of the different States.

The Reparation Commission would ask the Experts to give it, in all sincerity, their professional opinion on the questions submitted to them.

Monsieur Delacroix and I greatly hope that this further information may lead your Government to acquiesce in the acceptance by American Experts of the invitations which will be sent to them to participate in the labors of the committees. Furthermore, if you accept this suggestion, I am quite prepared to submit it to the Reparation Commission.

(Signed): Louis Barthou.

Mr. Logan's reply to M. Barthou:—

UNITED STATES UNOFFICIAL DELEGATION
REPARATION COMMISSION

Paris, 12 December 1923,
18 rue de Tilsitt.

My dear M. Barthou:—

I have not failed to inform my Government of your letter of December 5. My Government is deeply interested in the economic recuperation of Europe and is gratified to learn of the proposal for the establishment by the Reparation Commission of two Committees of Experts for the purposes stated. My Government notes the statement in your letter that the first committee of experts will endeavor to find:

(a) The means of balancing the budget of Germany, and

(b) The measures to be taken to stabilize its currency; and that to this end the experts will be invited to determine the conditions to be realized in order that a currency can be stabilized and the measures to be progressively taken so as to realize all of the conditions and also that they will be invited to study in detail the receipts and expenditures of the Reich as well as of the different states.

It has been made clear in our interviews that the Government of the United States is not in a position to be represented on these committees but my Government believes the proposed inquiries will be of great value and it views with favor the acceptance by American experts of invitations to participate in the work of the committees.

It is hoped that through these committees practicable and just solution of the pending problem may be found.

Faithfully yours,
(Signed) James A. Logan, Jr.

11, Old Broad Street,
London, E. C. 2½

31st December 1923.

I beg to acknowledge the receipt of your letter of the 26th instant inviting me to serve upon a Committee "entrusted with considering the means of balancing the (German) Budget and the measures to be taken to stabilize the currency."

I have been in consultation with Sir Josiah Stamp. As we understand the scope of the terms of reference they cover consideration of all the actual and potential sources of national revenue of Germany as an area defined by the Peace Treaty, and all the elements of national expenditure and obligation, whether definitive or not. In short, they omit nothing that is relevant to a complete and practical German Budget and to the establishment and maintenance of a stable currency.

We note that our interpretation is confined by the published correspondence between Monsieur Barthou and Mr. Logan.

In these circumstances I have the honour to accept your invitation.

I am, Sir,
Your obedient Servant,
(Signed) R. M. Kindersley.

The Secretary General,
Reparation Commission,
Paris.

APPENDIX NO. 2

RESOLUTIONS ADOPTED BY THE REPARATION COMMISSION ON NOVEMBER 30, 1923

In order to consider, in accordance with the provisions of article 234 of the Treaty of Versailles, the resources and capacity of Germany, and after giving her representatives a just opportunity to be heard, the Reparation Commission decides to create two committees of experts belonging to the allied and associated countries.

One of these committees would be entrusted with considering the means of balancing the budget and the measures to be taken to stabilize the currency.

The other would consider the means of estimating the amount of exported capital and of bringing it back to Germany.

MEMBERSHIP OF THE COMMITTEES

First committee

UNITED STATES:

Charles G. Dawes, Chairman.

Owen D. Young.

GREAT BRITAIN:

Sir Robert Molesworth Kindersley.

Sir Josiah Charles Stamp.

FRANCE:

Jean Parmentier.

Edgard Allix.

ITALY:
Alberto Pirelli.
Federico Flora.
BELGIUM:
Émile Francqui.
Baron Maurice Houtart.

Second committee

UNITED STATES:
Henry M. Robinson.
GREAT BRITAIN:
Reginald McKenna, Chairman.
FRANCE:
André Laurent-Atthalin.
ITALY:
Mario Alberti.
BELGIUM:
Albert-Edouard Janssen.

APPENDIX NO. 3

REPORT OF COMMITTEES OF EXPERTS TO REPARATION COMMISSION: COMPLETE OFFICIAL ENGLISH TEXT WITH ANNEXES

REPORT OF THE FIRST COMMITTEE OF EXPERTS

LETTER FROM THE CHAIRMAN TO THE REPARATION COMMISSION

APRIL 9, 1924.

Your Committee of Experts has unanimously adopted a report upon the means of balancing the budget of Germany and the measures to be taken to stabilize its currency, which I now have the honor to submit.

Deeply impressed by a sense of its responsibility to your commission and to the universal conscience, the committee bases its plan upon those principles of justice, fairness, and mutual interest, in the supremacy of which not only the creditors of Germany and Germany herself, but the world, has a vital and enduring concern.

With these principles fixed and accepted in that common good faith which is the foundation of all business and the best safeguard for universal peace, the recommendations of the committee must be considered not as inflicting penalties, but as suggesting means for assisting the economic recovery of all the European peoples, and the entry upon a new period of happiness and prosperity unmenaced by war.

Since, as a result of the war, the creditors of Germany are paying taxes to the limit of their capacity, so also must Germany pay taxes from year to year to the limit of her capacity. This is in accord with that just and underlying principle of the Treaty of Versailles, reaffirmed by Germany in her note of May 29, 1919, that the German scheme of taxation must be "fully as heavy proportionately as that of any of the powers represented on the commission." More than this limit could not be expected, and less than this would relieve Germany from the common hardship and give her an unfair advantage in the industrial competition of the future. This principle the plan embodies.

The plan has been made to include flexible adjustments which, from the very beginning, tend to produce the maximum of contributions consistent with the continued and increasing productivity of Germany. The conservative estimates of payments to be made in the near future are dictated by business prudence in outlining the basis of a loan, and should not destroy perspective as to the effects to be registered in the aggregate of eventual payments, which will annually increase. With normal economic conditions and productivity restored in Germany, most hopeful estimates of amounts eventually receivable will be found to be justified. Without such restoration, such payments as can be obtained will be of little value in meeting the urgent needs of creditor nations.

To insure the permanence of a new economic peace between the Allied Governments and Germany, which involves the economic readjustments presented by the plan, there are provided the counterparts of those usual economic precautions against default recognized as essential in all business relations involving expressed obligations. The existence of safeguards in no way hampers or embarrasses the carrying out of ordinary business contracts.

The thorough effectiveness of the safeguards should not embarrass the normal economic functioning of Germany, and is of fundamental importance to her creditors and to Germany.

Great care has been taken in fixing conditions of supervision over Germany's internal organization so as to impose the minimum of interference consistent with proper protection. This general plan, fair and reasonable in its nature, if accepted, leads to an ultimate and lasting peace. The rejection of these proposals by the German Government means the deliberate choice of a continuance of economic demoralization, eventually involving her people in hopeless misery.

In the preparation of this report, the committee has carefully and laboriously covered the broad field of investigation. It has had the constant cooperation of able staffs of experts, gathering information, digesting it and presenting it. It conducted, on the ground, an examination of the officials of the German Government and representatives of its labor, agriculture and industry. It received from the German Government and its representatives voluminous and satisfactory answers in response to its written inquiries. In connection with various features of its report, both for gathering information and for advice, it has called to its assistance outside experts of international reputation. The published reports and statements of economists of world-wide standing have been in its hands. It has had the benefit of the accumulated information heretofore gathered by your commission.

In its work, the full committee has held, since January 14, 1924, 54 meetings; the subcommittee on the stabilization of the currency, composed of Monsieur Parmentier, Sir Robert Kindersley, Monsieur Francqui, and Professor Flora, assisted by Mr. H. M. Robinson, under the chair-

manship of Mr. Owen D. Young, has held 81 meetings; and the subcommittee on the balancing of the budget, composed of Professor Allix, Baron Houtart, and Monsieur Pirelli, under the chairmanship of Sir Josiah Stamp, has held 63 meetings. They have had the assistance of Mr. Andrew McFadyean, the general secretary. Again, the time of the committee, outside of that consumed by the meetings, has been given largely to investigation and study.

In speaking of my colleagues and as bearing upon the value of this report, I feel that I should make it known to your commission and to the world, that their governments have in no case limited their complete independence of judgment and action, either before or after their appointment by you. Limited only by the powers granted by your commission, each has performed his arduous and responsible work as a free agent. These men, searching for truth and advice thereon, were answerable only to conscience. In granting this freedom, the governments have but followed your own spirit and intent in constituting the committee, but in so doing, they have paid the highest tribute which governments can bestow—complete confidence in a time of crisis in human affairs. In their vision, in their independence of thought, and above all, in their spirit of high and sincere purpose, which rises above the small things over which the small so often stumble, my colleagues have shown themselves worthy of this trust. That their work, which I now place in your hands, may assist you in the discharge of your great responsibilities, is their prayer and the knowledge hereafter, that it has done so, will be their full reward.

CHARLES G. DAWES, *Chairman.*

SUMMARY OF PART I*

I. The Attitude of the Committee

(a) The standpoint adopted has been that of business and not politics.

(b) Political factors have been considered only in so far as they affect the practicability of the plan.

(c) The recovery of debt, not the imposition of penalties, has been sought.

(d) The payment of that debt by Germany is her necessary contribution to repairing the damage of the war.

(e) It is in the interest of all parties to carry out this plan in that good faith which is the fundamental of all business. Our plan is based upon this principle.

(f) The reconstruction of Germany is not an end in itself; it is only part of the larger problem of the reconstruction of Europe.

(g) Guaranties proposed are economic, not political.

II. German Economic Unity

For success in stabilizing currency and balancing budgets, Germany needs the resources of German territory as defined by the Treaty of Versailles, and free economic activity therein.

III. Military Aspects; Contingent Sanctions and Guaranties

(a) Political guaranties and penalties are outside our jurisdiction.

*The summary is furnished only for the convenience of the readers. Parts I and II and the Annexes are the only authoritative statement of the plan.

(b) The military aspect of this problem is beyond our terms of reference.

(c) Within the unified territory, the plan requires that, when it is in effective operation:

1. If any military organization exists, it must not impede the free exercise of economic activities;
2. There shall be no foreign economic control or interference other than that proposed by the plan.

(d) But adequate and productive guaranties are provided.

IV. The Committee's Task

(a) Stabilization of currency and the balancing of budgets are interdependent, though they are provisionally separable for examination.

(b) Currency stability can only be maintained if the budget is normally balanced; the budget can only be balanced if a stable and reliable currency exists.

(c) Both are needed to enable Germany to meet her internal requirements and treaty payments.

V. Economic Future of Germany

(*a*) Productivity is expected from increasing population, technical skill, material resources, and eminence in industrial science.

(b) Plant capacity has been increased and improved since the war.

VI. Currency and a Bank of Issue

(a) All classes will benefit from stabilized currency, especially labor.

(b) Under present conditions rentenmark stability is only temporary.

(c) A new bank is set up or the Reichsbank reorganized.

(d) The main characteristics of the bank will be:

1. To issue notes on a basis stable in relation to gold, with an exclusive privilege;
2. To serve as a banker's bank, establishing the official rate of discount;
3. To act as the Government banker, but free of Government control;
4. Advances to Government to be strictly limited;
5. To hold on deposit reparation payments;
6. The capital of the bank will be 400,000,000 gold marks.
7. It will be directed by a German president and managing board, who can be assisted by a German consultative committee;
8. The due observance of its statutes will be further safeguarded by a general board, of which half of the members, including a commissioner, will be foreign.

VII. Budget and Temporary Reparation Relief

Balancing the German budget requires:

(a) Full economic and fiscal sovereignty, subject to the supervision provided for in this report;

(b) A stable currency;

(c) Temporary relief from charges on the budget for treaty obligations;

(d) Such relief not to suspend essential deliveries in kind.

VIII. The Basic Principles of Germany's Annual Burden

(a) Treaty obligations and continuity of balanced budgets.

1. Balancing the budget does not entail merely provision for internal administrative expenditure.
2. Germany must also provide within the utmost limit of her capacity for her external treaty obligations.
3. The budget can be balanced without necessarily dealing with the total capital debt of Germany.
4. It can not be continuously balanced unless the annual charge is fixed for a considerable period, on a basis clearly prescribed in advance.

(b) Commensurate taxation.

1. Government internal debt has been practically extinguished by the depreciation of the currency.
2. New debt charge ought to be met commensurate with the burden of the French, English, Italian, and Belgian taxpayer.
3. The treaty recognizes this principle.
4. It is morally sound.
5. It is economically just in its influence on costs of production.
6. This principle has been applied to the full limit of practicability.

(c) Allies' share in Germany's prosperity.

1. Germany's creditors must share in the improvement in Germany's prosperity.
2. This will be secured by an index of prosperity.

(d) There is an important difference between the Germans' capacity to pay taxes and Germany's capacity to transfer wealth abroad.

IX. Normal Resources from Which Payments Are Made

Germany will pay treaty charges from three sources: (A) Taxes; (B) Railways; (C) Industrial debentures.

(A) From her ordinary budget.

1924-25 budget may be balanced if it is free from peace treaty charges.

1925-26 budget receiving 500,000,000 gold marks from special sources, may pay that sum for reparation.

	Gold marks
1926-27	*110,000,000
1927-28	*500,000,000
1928-29	1,250,000,000

This is considered a normal year and a standard payment; thereafter additional payments will be made, depending on prosperity.

(B) From Railways:

1. Railway bonds—

(a) Eleven milliards of first mortgage railway bonds against a capital cost of twenty-six milliards will be created for reparations;

(b) These bonds bear 5 per cent interest and 1 per cent sinking fund per annum;

(c) In view of reorganization, interest is accepted as follows:

	Gold marks
1924-25	330,000,000
1925-26	465,000,000
1926-27	550,000,000
1927-28 and thereafter	660,000,000

Behind the bonds there will be created 2 milliards of

*Subject to addition or reduction in certain contingencies.

preference shares to be reserved for sale to the public, and 13 milliards of common stock; three-fourths of the proceeds of the preference shares will be applied, as required, to the payment of debt and for capital expenditure of the railways. The remaining 500 millions of preference shares and all the common shares go to the German Government.

2. Transport tax—

After 1925-26, 290,000,000 gold marks per annum for reparation and balance to German Government.

(C) Industrial debentures.

1. Five milliards of industrial debentures are provided for reparation.
2. The resulting charge on industry is less than that existing before the war and now wiped out by depreciation.
3. These bonds bear 5 per cent interest and 1 per cent sinking fund, i. e., 300,000,000 gold marks per annum.
4. Pending economic restoration, interest and sinking fund are accepted as follows:

   First year: Nothing.
   Second year: 125,000,000 gold marks.
   Third year: 250,000,000 gold marks.
   Thereafter: 300,000,000 gold marks.

X. Summary of Provision for Treaty Payments

(a) 1. Budget moratorium period.

First year: From foreign loans and part interest on railway bonds:

	Gold marks
Total.....	1,000,000,000

Second year: From part interest on railway bonds and

on industrial debentures, budget contribution, through sale of 500,000,000 gold mark railway shares:

	Gold marks
Total	1,220,000,000

2. Transition period.

Third year: From interest on railway bonds and on industrial debentures, from transport tax, and from budget:

	Gold marks
Total	1,200,000,000

subject to contingent addition or reductions of 250,000,000 gold marks.

Fourth year: From interest on railway bonds and on industrial debentures, from transport tax, and from budget:

	Gold marks
Total	1,750,000,000

subject to contingent addition or reduction of 250,000,000 gold marks.

3. Standard year.

Fifth year: From interest on railway bonds and on industrial debentures, from transport tax, and from budget:

	Gold marks
Total	2,500,000,000

Thereafter, 2,500,000,000 plus a supplement computed on the index of prosperity. Interest on the securities, but not the proceeds of their sale, is included in these figures.

(b) The first year will begin to run from the date when the plan shall have been accepted and put into effective execution.

XI. Inclusive Amounts and Deliveries in Kind

(a) The above sums cover all amounts for which Germany may be liable to the Allied and Associated Powers.

(b) Deliveries in kind are to be continued, but are paid for out of balances in the bank.

XII. How the Annual Payments Are Made by Germany

(a) The amounts will be raised in gold marks and paid into the bank.

(b) These payments cover Germany's annual obligation.

XIII. How the Payments Are Reduced by the Creditors

(a) Germany's creditors will use these moneys in Germany or convert them into foreign currencies.

(b) Experience will show the rate and extent to which the conversion can safely take place.

(c) Danger to stability through excessive remittances is obviated by a transfer committee.

(d) Sums not remitted accumulate, but with a limitation of amount.

XIV. Guaranties, in Addition to Railway and Industrial Bonds

(a) The following revenues are pledged as collateral security for budget contributions and other payments: Alcohol, tobacco, beer, sugar, customs.

(b) The yield of these revenues is estimated to be substantially in excess of required payments.

(c) The excess is returned to the German Government.

XV. External Loan—Its Conditions and Purpose

Foreign loan of 800,000,000 gold marks meets a double purpose.

(a) Requirements of gold reserve of the new bank.

(b) Internal payments for essential treaty purposes in 1924-25.

XVI. Organization

The organization consists of:

(a) A trustee for railway and industrial bonds;

(b) Three commissioners of (1) railways, (2) the bank, (3) controlled revenues;

(c) An agent for reparation payments, who will coordinate the activities of the above and will preside over the transfer committee.

XVII. The Nature of the Plan

(a) The plan is an indivisible unit.

(b) The aim of the plan is; (1) To set up machinery to provide the largest annual payments from Germany; (2) To enable maximum transfers to be made to Germany's creditors; (3) To take the question of "what Germany can pay" out of the field of speculation and put it in the field of practical demonstration; (4) To facilitate a final and comprehensive agreement upon all the problems of reparations and connected questions, as soon as circumstances make this possible.

TEXT OF THE REPORT

We were invited by the Reparation Commission, by decision of November 30, 1923, to "Consider the means of balancing the budget and the measures to be taken to stabilize the currency" of Germany.

We have been in continuous session since January 14, 1924, in Paris, except for one fortnight spent in Berlin.

We have called in to assist us eminent technical advisers on the various questions which have been under consideration, and have been in touch with representative German opinion.

We have the honor to present the following report which states the unanimous conclusions formed as a result of our studies and inquiries.

Part I of this report states our conception of our task, our conclusions, and the broad outline of our plan.

Part II indicates the considerations which guided us to our conclusions, in particular so far as they result from certain aspects of the present financial and economic condition of Germany, which is here described.

Part III consists of a series of annexes which give the technical detail of our several proposals, and should be read as a supplement to the respective portions of Part I.

PART I.—THE COMMITTEE'S CONCLUSIONS AND SCHEME

I. The Attitude of the Committee

We have approached our task as business men anxious to obtain effective results. We have been concerned with

the technical and not the political aspects of the problem presented to us. We have recognized indeed that political considerations necessarily set certain limits within which a solution must be found if it is to have any chance of acceptance. To this extent, and to this extent only, we have borne them in mind.

The dominating feature of the German Budget is Germany's obligation to the Allies under the Treaty of Versailles. We have been concerned with the practical means of recovering this debt, not with the imposition of penalties and the guarantees which we propose are economic and not political. At the same time it is no ordinary debt with which we deal, for Germany suffered no appreciable devastation, and her primary moral obligation is toward those who have suffered so severely through the war.

As regards past history, it has not seemed necessary to establish the causes, nor the responsibility for those causes, which have operated to produce the present state of German finances and currency, except in so far as a recognition of their character is required for the prescription of remedies.

Finally, convinced as we are, that it is hopeless to build any constructive scheme unless this finds its own guarantee in the fact that it is to the interest of all the parties to carry it out in good faith, we put forward our plan relying upon this interest. We hope the character of our plan will itself assist in securing this guarantee, which is essential for its execution; but in the main, of course, it must be for others to take such measures as are necessary to maintain or assure it.

II. German Economic Unity

The committee has had to consider to what extent the balancing of the budget and the stabilization of the cur-

rency could be reestablished permanently in Germany as she actually is at the present moment, with limitations as to her fiscal and economic rights over part of her area.

We should say at the outset that we have been unable to find any practical means of ensuring permanent stability in budget and currency under these conditions, and we think it unlikely that such means exist. The solution of the double problem submitted to us implies indeed the restoration of Germany's credit both externally and internally, and it has appeared to us impossible to provide for this restoration under the conditions mentioned. We have, therefore, been compelled to make the assumption that the fiscal and economic unity of the Reich will be restored and our whole report is based on this hypothesis.

III. Military Aspects—Contingent Sanctions and Guarantees

If political guarantees and penalties intended to insure the execution of the plan proposed are considered desirable, they fall outside the committee's jurisdiction.

Questions of military occupation are also not within our terms of reference.

It is, however, our duty to point out clearly that our forecasts are based on the assumption that economic activity will be unhampered and unaffected by any foreign organization other than the controls herein provided. Consequently, our plan is based upon the assumption that existing measures, in so far as they hamper that activity, will be withdrawn or sufficiently modified so soon as Germany has put into execution the plan recommended, and that they will not be reimposed except in the case of flagrant failure to fulfill the conditions accepted by common agreement. In case of such failure it is plainly for the creditor Governments, acting with the conscious-

ness of joint trusteeship for the financial interests of themselves and of others who will have advanced money upon the lines of the plan, then to determine the nature of sanctions to be applied and the method of their rapid and effective application.

In saying this we wish to add at once that if the economic system now in operation in occupied territory is modified, we are unanimously of the opinion that a settlement of reparation must be reinforced by adequate and productive securities. We propose for this purpose a system of control which we believe will be effective, and at the same time such as not to impede the return to financial stability (see XIV below).

IV. The Committee's Task

As the terms of reference indicate, two principal problems were submitted to us for inquiry—the stabilization of German currency and the balancing of the German budget. It is self-evident that these problems are interdependent. The currency of a country can not remain stable unless its budget is normally balanced, for if expenditure continually exceeds receipts there will in time be no alternative to the printing of new notes to meet the excess; and the inflation will inevitably involve depreciation. On the other hand, the task of balancing a budget, unless the currency is relatively stable, is an impossible one, for a falling currency makes calculations both of receipts and expenses unreliable, and in particular causes a continual loss to the taxing authority through the necessary interval of time between assessment and collection. While, therefore, in the nature of things it is necessary that the two problems should in the first instance be studied separately—their interdependence must be consistently borne in mind. In examining each of them separately, we have assumed for the minute that the other

has been solved, without ever losing sight of the fact that the stabilization of the currency and the balancing of the budget are means designed to enable Germany to satisfy her own essential requirements and to meet her Treaty commitments, the fulfillment of which is so vital to the reconstruction of Western Europe. It must not be forgotten that the performance of these commitments is of vital importance, not only for the countries having a claim on Germany, but also for Germany herself. It is, indeed, clear that a Germany whose economy had again become flourishing could not long resist a financial and economic crisis in the nations surrounding her. In order that the restoration of Germany may be definitive, the other nations must also return to the conditions requisite for their financial and economic existence and must likewise be enabled to carry on the normal exchange of goods on which the general prosperity depends.

V. The Economic Potentialities of Germany

The task would be hopeless if the present situation of Germany accurately reflected her potential capacity; the proceeds from Germany's national production could not in that case enable her both to meet the national needs and to insure the payment of her foreign debts.

But Germany's growing and industrious population; her great technical skill; the wealth of her material resources; the development of her agriculture on progressive lines; her eminence in industrial science; all these factors enable us to be hopeful with regard to her future production.

Further, ever since 1919 the country has been improving its plant and equipment; the experts specially appointed to examine the railways have shown in their report that expense has not been spared in improving the German railway system; telephone and telegraph

communications have been assured with the help of the most modern appliances; harbors and canals have likewise been developed; lastly, the industrialists have been enabled further to increase an entirely modern plant which is now adapted in many industries to produce a greater output than before the war.

Germany is therefore well equipped with resources; she possesses the means for exploiting them on a large scale; when the present credit shortage has been overcome, she will be able to resume a favored position in the activity of a world where normal conditions of exchange are gradually being restored.

Without undue optimism, it may be anticipated that Germany's production will enable her to satisfy her own requirements and raise the amounts contemplated in this plan for reparation obligations. The restoration of her financial situation and of her currency, as well as the world's return to a sound economic position, seem to us essential but adequate conditions for obtaining this result.

VI. Stability of the Currency—A New Bank of Issue

We propose to deal in the first place with the currency problem.

The present financial and currency position in Germany is stated in Part II. It will be seen that by means of the rentenmark, stability has been attained for a few months, but on a basis which, in the absence of other measures, can only be temporary.

The committee proposes the establishment of a new bank of issue in Germany, or, alternatively, a reorganization of the Reichsbank, as an essential agency for creating in Germany a unified and stable currency. Such a currency, the committee believes, is necessary for the rehabilitation of Germany's finances, the balancing of her budget and the restoration of her foreign credit. The principal

features of the bank plan, which is printed in Annex 1, are as follows:

The bank is to have the exclusive right (with certain minor qualifications) to issue paper money in Germany for the period of its charter, fifty (50) years. All of the many kinds of paper money now circulating in Germany (except limited note issues of certain State banks) are to be gradually withdrawn from circulation, giving place to a single uniform paper currency, the bank-notes of the new bank. These bank-notes will be protected by a normal legal reserve of thirty-three and one-third per cent, and by other liquid assets. The reserve will be held largely in the form of deposits in foreign banks.

The plan contemplates that as a permanent policy the notes of the bank shall be redeemable in gold, but the committee is of the opinion that at the time of the inception of the bank the situation will temporarily not allow of the application of the rule of convertibility. It therefore suggests that a currency should be created which will be kept stable in relation to gold and as soon as conditions permit be placed on a convertible basis.

Like the present Reichsbank, the new bank will serve as a bankers' bank, rediscounting the safest category of short-term bills, etc., and so establishing the official rate of discount. It will also handle for the other banks the giro system for the transfer of bank credits.

The bank will deal with the public, making short-time commercial loans and discounts, effecting transfers, and receiving deposits.

It will be the depository and the fiscal agent of the German Government. It may make short-term loans to the Government, but the amount and character of these loans are strictly limited, and the granting of such loans is carefully safeguarded. The German Government is to participate in the profits of the bank but the bank is to be entirely free from governmental control or interference.

Treaty funds collected in Germany are all to be deposited in the new bank to the credit of a special account and are only to be withdrawable by the creditor nations under conditions and safeguards which will adequately protect the German exchange market and the interests of the creditor nations and the German economy.

The new bank will have a capital of four hundred million (400,000,000) gold marks, part to be subscribed in Germany and part abroad. It is to be administered by a German president and a German managing board, which can have the assistance, as in the case of the Reichsbank, of a consultative committee. Alongside of this German managing board there is to be another board, called the "General Board," which will consist of seven Germans and seven foreigners, one each of the following nationalities; British, French, Italian, Belgian, American, Dutch and Swiss. This general board is given broad powers in such matters of bank organization and operation as might affect the interests of the creditor nations. One of the foreign members of the general board will be known as the "commissioner." He will be responsible for seeing that there is no infringement of the provisions relative to the issuance of notes and the maintenance of the bank's reserves. Decisions of the general board will require a majority vote of ten of the fourteen members, unless both the president and the commissioner are included in the majority, in which case a simple majority will be sufficient. Thus, cooperation by members of both groups is necessary for action.

It has been suggested in various quarters that to ensure the bank's independence of the Government, an issue department, which could be under the direction of the commissioner and which would be responsible for the reserve and for the issue of notes, should be established abroad. Such a guarantee is political rather than technical in char-

acter, and to propose it is outside the jurisdiction of the committee.

A study of the annex is essential to a thorough comprehension of the committee's recommendations, and it has contented itself with drawing attention here to the main features to which it attaches importance.

Still assuming for the minute that the budget problem has been successfully surmounted, we believe that our recommendations furnish a practical method, not only of stabilizing the German exchange, but of securing to German economy those credits in stable value which are essential to its reinvigoration and to the payment of reparation.

Labor also will benefit, for its interests above all are dependent upon stability. Some classes of the community may have compensations in the amazing overturn of fortunes which inflation brings—some benefit and others suffer. But for the working classes instability is wholly evil; it has no compensation whatever. In this connection, we may refer to the views expressed by the representative of labor who appeared before us in Berlin: "speaking not for the whole of the German people, but merely for the class which he represented, Herr Grassman stated that the German working classes could not stand another period of inflation. They must appeal to the world for a stable currency which would render it possible for them to buy something with their wages even four weeks after they had received them." It is clear that if the statutes of the bank are strictly observed there can be little danger of future inflation. One of the advantages to be expected is that foreign currencies immobilized in Germany, which are at present economically sterile, will be mobilized in the form of subscriptions or deposits to the bank and return to economic uses.

VII. The Budget and Temporary Reparation Relief

Attention may now be directed to the other main aspect of our problem, the balancing of the budget. We propose to deal first with the general budget of the Reich, and secondly and separately with the railways, which at present are contributing nothing to the general budget.

In addition to a stable currency and the economic unity defined above, the budget requires certain relief from immediate charges for treaty purposes, which, while securing the budgetary position, will not imply the cessation of the payments indispensable to the Allies in the form of deliveries in kind.

VIII. The Basic Principles of Germany's Annual Burden

(*a*) treaty obligations and their bearing upon the continuity of balanced budgets

It will be obvious that the balancing of the budget is, like the stabilization of the currency, of little value unless it can be maintained. It is not enough to be satisfied that one or even several budgets will be balanced. It is necessary to consider under what conditions, assuming sound administration, financial as well as currency stability can be continuously insured, or rather under what conditions such stability once gained is likely to be endangered. It is inevitable, therefore, that we should look forward, not indeed in the same detail but with proper regard to the chief determining factors, to those later years during which Germany will have gradually to liquidate her external treaty obligations.

We repudiate, of course, the view that Germany's full domestic demands constitute a first charge on her resources and that what is available for her treaty obligations is

merely the surplus revenue that she may be willing to realize. But at the same time, if the prior obligation for reparation that is fixed for Germany to pay, together with an irreducible minimum for her own domestic expenditure, make up in a given year a sum beyond her taxable capacity, then budget instability at once ensues and currency stability is also probably involved. In that event, an adjustment of the treaty obligations of the year is obviously the only course possible. The amount that can safely be fixed for reparation purposes tends therefore to be the difference between the maximum revenue and minimum expenditure for Germany's own needs. We shall naturally and inevitably be led to discuss later the amount of reparation payments which can be made out of budget resources and the method by which they can be effected, if the postulates of a stable currency and of a balanced budget are accepted. It would be to ignore both the plain dictates of justice, the practical conditions which must determine the acceptance or rejection of our proposals, and the context and obvious purpose of our terms of reference, if we approached our task from any other angle.

It might, indeed be thought that if we have thus been involved in a consideration of reparation payments, it is only of such payments as are to be made during the reconstruction period of the next few years. Our task, it may be said, is to advise as to the way to attain stabilization and a balanced budget, not as to the sums to be demanded from Germany when that aim has been achieved. But no such sharp division of periods is possible, for the following reasons:

1. The basis on which the budget is balanced at the end of the reconstruction period, and the sum it includes for reparation, must obviously determine to a large extent the sums payable in the following years. Otherwise, as we have said, an equilibrium, though once attained, might

be rapidly lost. The effort would have been in vain and the same problem would again present itself.

2. More important still is the fact that the success of our proposals to attain financial stabilization depends essentially upon the return of confidence. Without this the return of German capital invested abroad, the attraction of foreign capital for the purposes mentioned in the scheme and of foreign credits for the current conduct of business, and even the proper collection of taxes, will alike be impossible.

Such confidence can not be attained unless a settlement is now made which both Germany and the outside world believe will give an assurance that for a considerable period neither its finances nor its foreign relations will be endangered by renewed disputes. Such an assurance, as we shall see, does not mean making the charge on Germany a uniform one over a period of years, nor even deciding beforehand what the charge shall be in each of these years. But it does mean settling beforehand the method by which increases shall be determined.

When we speak of the adoption of such a method for "a considerable period," we are thinking primarily of the period which lenders and investors whose money is required as a part of our scheme will have in mind. As we shall see, our scheme needs both foreign and internal subscriptions to a bank of issue, and in particular an external loan as an essential condition of enabling and assuring reparation payments. We fully recognize both the necessity and the justice of maintaining the principle embodied in the treaty that Germany's payments should increase with what may prove to be the increase in her future capacity.

We also recognize that an estimate now made once for all might well underestimate this, and that it is both just and practicable that the Allies should share in any in-

creased prosperity. All that we regard as essential as a condition of stabilization is that any such increased demands to correspond with increasing capacity should be determined by a method which is clearly defined in the original settlement, and which is capable of automatic, or at least professional, impartial, and practically indisputable application.

This requirement we have tried to meet, as will be seen, by providing that in addition to a fixed annual payment, there shall be a variable addition dependent upon a composite index figure designed to reflect Germany's increasing capacity.

It is outside the competence of the committee to establish a limit of years or of amount for the working of the index, nor is it within their competence to fix the number of annuities which Germany will have to pay, as this would practically mean the fixation of a new German capital debt. In any new arrangements made for a definite settlement of the various international financial obligations arising out of the war it would be easy as regards the German debt to apply our plan to those new conditions.

(b) COMMENSURATE TAXATION

We have done our utmost to apply the principle of commensurate taxation.

It is not open to dispute, as a simple principle of justice, and it is contemplated by the treaty, that the German people should be placed under a burden of taxation at least as heavy as that borne by the peoples of the Allied countries. No single person in Germany, whether speaking as an individual or representing any section of the nation, has failed to accept that principle when it has been squarely put to him. Any limitation upon it, if there is one, must be a limitation of practicability and general

economic expediency in the interest of the Allies themselves. Obviously it is morally sound; and it would be clearly repugnant to all sense of natural justice that the taxpayers of countries with large and important regions devastated by the war should bear the burden of restoring them, while the taxpayer of Germany, on whose territory the war caused no comparable devastation, escaped with a lighter burden. The principle is, at the same time, economically just, for it is obviously unfair and in every way undesirable that the allied taxpayer should be penalized by the fact either that taxes resulting from the war weigh more heavily upon him as a consumer, or that in competition in his business he should be handicapped by greater burdens on the costs of production, including wages, than his German competitor bears.

We have borne in mind both the importance of the virtual extinction of debt in Germany and the general burden of taxation in allied countries. As we indicate more fully in Part II, there are many difficulties in theory and practice, but in spite of them we have done our utmost to secure that the proposals we make should involve a "commensurate burden" in the fairest interpretation and application of that principle which is practicable. We are satisfied that in what we propose we are not imposing a heavier burden; we are also satisfied that we have applied the principle as far as it is practicable in the interests no less of the Allies than of Germany.

(c) AN INDEX OF PROSPERITY IS NECESSARY TO ENABLE THE ALLIES TO SHARE IN THE INCREASED PROSPERITY OF GERMANY

After a short period of recovery we believe that the financial and economic situation of Germany will have returned to a normal state, after which time the index will begin to operate.

The system of a variable annuity has the sanction of usage in the schedule of payments. But we venture to suggest for most careful consideration the advisability of altering the existing index, constituted by the value of exports. This index appears to us to be imperfect.

We are aware that there are cogent reasons both for and against any test which may be suggested, and we do not propose to examine them in detail. We are of opinion that the undoubted shortcomings of particular indices are neutralized to a large extent if a composite index is chosen, and we have a reasonable assurance that a fair measure of Germany's increasing prosperity will be obtained. Our suggestions, after considering many various alternatives for such an index, are given in Annex 2.

We take upon ourselves to recommend these suggestions, as an indication, to the attention of the Reparation Commission.

We are of opinion that at least during the period within which the loan which we propose is being amortized, the annual charge upon Germany should not be heavier than that which would result from the application of this index; nor would the committee accept any responsibility for the balancing of the budget even in later years if heavier payments than the above were called for.

We propose that an average of years (chiefly 1926, 1927, 1928, and 1929) should be taken as the base; that the percentage increase shown by each of six sets of representative statistics (railway traffic, population, foreign trade, consumption of tobacco, etc., budget expenditure, and consumption of coal) should be ascertained; and that the average of these six percentages should be taken as indicating the proportionate increase to be added to the treaty sums demanded in a given future year.

Under this system Germany will retain her incentive to develop, as she retains the major part of the advantage

of any increase in prosperity, while the Allies obtain a reasonable share in this increase and avoid the risk of losing through a premature estimate of future capacity.

At the same time, the adoption of a method involving not discretionary but automatic application gives the necessary assurance from the commencement both to Germany and the world that treaty demands will not, in the period to which the settlement relates, be again the subject of negotiation and dispute.

We propose, however, one further correcting factor of quite a different character which is only a precautionary measure and may never be actually involved. The treaty prescribes Germany's obligations in terms of gold, and for convenience we have expressed our estimate in the same terms. But both the burden on Germany, and the advantage to the Allies of treaty payments, consist of goods and services. Gold is only a measure of value, and over a long period of years may be an uncertain and defective one. It is only in the case of really important changes that any action is necessary and we therefore propose that a reduction or increase of the figures both as regards the standard and the supplementary payments should be made automatically in correspondence with changes in the general purchasing power of gold, whenever, by the decision of an impartial authority, such changes amount to more than 10 per cent.

(d) THE DISTINCTION BETWEEN THE TAXPAYERS' "CAPACITY TO PAY" IN GERMANY AND GERMANY'S CAPACITY TO PAY THE ALLIES

There has been a tendency in the past to confuse two distinct though related questions; i. e., first, the amount of revenue which Germany can raise available for reparation account, and, second, the amount which can be

transferred to foreign countries. The funds raised and transferred to the Allies on reparation account can not, in the long run, exceed the sums which the balance of payments makes it possible to transfer, without currency and budget instability ensuing. But it is quite obvious that the amount of budget surplus which can be raised by taxation is not limited by the entirely distinct question of the conditions of external transfer. We propose to distinguish sharply between the two problems, and first deal with the problem of the maximum budget surplus and afterwards with the problem of payment to the Allies. In the past the varying conclusions formed as to Germany's "capacity" have often depended upon which of these two methods has been chosen.

As a first method of approach the budgetary criterion has obvious advantages and attractions. Reparation must first be provided for as an item in the budget.

The budget itself is the sum of decisions taken by a single authority. It is capable of expert judgment and, within narrower limits of error, of calculation and analysis.

By comparison a country's "economic balance" defies exact calculation. The balance, even at a given moment, can only be estimated approximately, for the invisible exports and imports which constitute an important part of it can not be known exactly. And a *potential* economic balance is much more uncertain. It depends not on the decisions of a single authority, but on the enterprise of individual merchants and manufacturers. Reparation demands themselves will increase it. The extent to which economic adaptation is possible over a long period of years, under the pressure of external obligations, is a matter of conjecture; an existing economic balance, before such obligations have been in operation long enough to have their effect on the economy of the country, gives a

very uncertain criterion. The economic balance is, therefore, by comparison with the budget, incapable of close calculation, "unmanageable," and too elastic.

But the limits set by the economic balance, if impossible of exact determination, are real. For the stability of a country's currency to be permanently maintained, not only must her budget be balanced, but her earnings from abroad must be equal to the payments she must make abroad, including not only payments for the goods she imports, but the sums paid in reparation. Nor can the balance of the budget itself be permanently maintained except on the same conditions. Loan operations may disguise the position—or postpone its practical results—but they can not alter it. If reparation can, and must, be provided by means of the inclusion of an item in the budget, i. e.: by the collection of taxes in excess of internal expenditure, it can only be paid abroad by means of an economic surplus in the country's activities.

We have, it will be seen, attempted to give effect to both these sets of considerations by a method we believe to be both logical and practical. We estimate the amount which we think Germany can pay in gold marks by consideration of her budget possibilities; but we propose safeguards against such transfers of these mark payments into foreign exchange as would destroy stabilization and thereby endanger future reparation.

By comparison with a system which reduced the sums considered possible on budget grounds because of considerations based upon estimates of the possible economic balance, this has the following advantages:

(a) It enables the maximum sums to be obtained and paid to the Allies' account.

(b) Any limitation upon transfers into foreign currencies will depend upon the exact economic position as it

develops in fact and not upon a necessarily problematical estimate of it; and the limitation will only apply so far as it actually proves necessary.

(c) Even so far as the sums paid in reparation can not be completely transferred, they can, under certain conditions, be used by the Allies for internal investment in Germany.

Above all, we recommend our proposal for these reasons: It adjusts itself automatically to realities; the burden which should rest upon the German taxpayer should, in justice, so obviously be commensurate with that borne by the Allied taxpayer that, in our view, nothing but the most compelling and proved necessity should operate to make it lighter. It would be both speculative and unjust to attempt to forecast the possibilities of the future exchange position and to determine Germany's burden in advance with reference to a problematic estimate of it. Experience and experience alone, can show what transfer into foreign currencies can in practice be made. Our system provides in the meantime for a proper charge upon the German taxpayer, and a corresponding deposit in gold marks to the Allies' account; and then secures the maximum conversion of these mark deposits into foreign currencies which the actual capacity of the exchange position at any given time renders possible.

IX. The Normal Resources from Which Germany Should Make Payments

With these principles in mind, we recommend that Germany should make payment from the following sources:

(a) From her ordinary budget.

(b) From railway bonds and transport tax.

(c) From industrial debentures.

We proceed to consider each of these in turn.

(a) PROVISION FROM THE BUDGET FOR TREATY PAYMENTS; BUDGET EQUILIBRIUM

To recommend what payments Germany can make from her ordinary budget, and from what dates, is in effect to answer the first of the two specific questions put to us; i. e., how to "balance the German budget." For in our view, if the economic and fiscal unity of the Reich is restored, if a stable currency is established, and if the budget is given temporary relief from treaty payments, Germany should balance her budget from her own resources by a vigorous internal effort supported by the confidence which a general and stable settlement may be expected to give, and she should thereafter be able to maintain it in equilibrium, if the future charge for treaty payments is determined by a method which assures that it will not exceed her capacity.

In other words, we do not consider that an external loan is needed—as in the case of Austria and Hungary—to be devoted specifically to meeting ordinary deficits during a transition period. External money is indeed an essential part of our scheme, in part for the establishment of a new bank of issue; in part to prevent an interruption of deliveries in kind during the transition period; and essentially to create the confidence upon which the whole success of the scheme depends. But we do not propose that it should be confined or devoted specially to meeting deficits on ordinary expenditure even during a transition period. On the contrary, as will be seen, we think that from the beginning internal resources should meet internal ordinary expenditure, and at a very early date should suffice in addition to make substantial contributions toward the external debt.

The present budget position is described in some detail in Part II, which includes our criticisms and recommenda-

tions as to the measures we think practicable for economizing in expenditures and increasing taxation.

We confine ourselves here to our conclusions as to the provision that can be made for meeting treaty payments.

1924-25 budget.—In the first year (1924-25) we consider that the ordinary budget may balance. Even if there is a deficit we are confident that it should not be such as to endanger the stability of the currency, and that at the worst the Government can meet it by the orthodox expedients—increases of existing taxation, further emergency taxes, and internal loans.

Even if energetic measures are taken to obviate any deficit in 1924-25, we are satisfied that neither by reduction of expenditures nor by an increase in receipts can Germany be expected to provide out of budget resources for any peace treaty payments to the Allies, and that any demand for their payment would imperil both the structure of the budget and the stability of the currency. How relief can be otherwise provided for the reparation creditors will be considered separately.

The fundamental importance of the effect upon the stability of the Reich budget of the finances of the States (Prussia, Bavaria, etc.) and of the communes has greatly exercised us, and we have stated our views on the system of subsidies and local expenditure in Part II.

1925-26 budget.—On passing to the budget for 1925-26, it is obvious that the existing data are insufficient for a precise judgment on its detailed prospects. Certain general conclusions are, however, possible.

On the revenue side, the lapse of a whole year of currency stability and readjustment should of itself increase receipts. The period of recuperation will not have been long enough completely to restore the yield of the income tax, but there will at least be gold mark profits of 1924-25

on which to frame a reasonable assessment. Consumption taxes should be directly affected by returning prosperity.

On the expenditure side it may be hoped with some degree of confidence that expenditure on unemployment will exhibit a notable decrease. The expenditure on the army is capable of reduction. An automatic decrease will make itself felt in the pension charge. It is not to be expected, on the other hand, that sums thus saved on these or other heads will represent a net benefit to the budget. In particular, and this remark applies also to the budgets of the immediately succeeding years, increases in the salary charges of the Reich which can probably not be entirely off-set by decreases in personnel must be anticipated.

Some increase of expenditure must therefore be expected. On the balance, however, we are of opinion that the growth in receipts should be more than sufficient to counterbalance any increase in expenditure. Whatever views may be held about the eventual outcome of the 1924-25 budget, we are clear that the second year should show a substantial improvement upon it. The result of the first year therefore affects our view as to whether the result of the following year will be actually an appreciable surplus. If it should prove that the 1924-25 budget can not be balanced by taxation alone, the improvement to be expected in the following year might not be more than sufficient to secure the balance desired. If, on the other hand, no loans were necessary in 1924-25, any improvement in the following year would be net surplus and entirely available for meeting peace treaty charges.

We are clearly of the view that, if the two years are taken together, receipts should be sufficient to cover ordinary expenditure, and we do not exclude the possibility of a small surplus. On the other hand it can not be stated with certainty that the inclusion of a compulsory

liability for peace treaty charges will not destroy the whole balance, and it is obviously vital that the mistake should not be made of fixing as a first payment during recovery a sum which the circumstances may not justify.

The stability of future reparation payments and German credit in general might thus be endangered.

There is another factor that must be taken into account. For the successful operation of the scheme for dealing with the railways, to which we shall refer later, it is necessary that the proceeds of the transport tax to the extent of 250,000,000 gold marks should be withdrawn for this year from the revenue side of the budget and devoted to the payment of treaty charges.

On the other hand that scheme also provides for the sale by the railway company of preference shares to the nominal value of 2,000,000,000 gold marks, one-quarter of the proceeds accruing to the profit of the German budget and the balance providing for past and future capital expenditure of the railways. For the successful execution of the railway scheme we attach great importance to the sale to the public of these preference shares and we feel justified in assuming that before the end of the year 1925-26 the German Government will be in effective possession of 500,000,000 gold marks as a result of this transaction. The budget can therefore be reinforced to that extent and after making allowance for the withdrawal of 250,000,000 gold marks in respect of the transport tax there will be a balance of 250,000,000 gold marks which should be available for meeting peace treaty charges.

By the procedure we have indicated any danger of hampering future stability by a premature call upon the ordinary resources of the German budget will be obviated and there will be an additional inducement to transfer the preference shares to private ownership.

We, therefore, recommend that in the year 1925-26 Germany should be required to meet peace treaty charges out of her budget to the extent of 250,000,000 gold marks. If, contrary to our expectations, the budget fails to realize 500,000,000 gold marks from the sale of preference shares, we consider that any resultant deficit could be met by an internal loan.

The proceeds of the transport tax should thenceforth not figure in the revenue side of the budget except to the extent to which they exceed 250,000,000 gold marks in 1925-26 and 290,000,000 gold marks in subsequent years.

We once more reserve the question of providing for further reparation payments by other means.

The budget of later years.—As we have said already, Germany's credit can not rest upon the mere establishment of budget equilibrium. It must be clear that it can be permanently maintained. It is, therefore, necessary for us to consider what burden Germany can bear in the near future without danger to that equilibrium. In this connection, certain assumptions have necessarily been made. It has been considered that if for two years the budget is relieved from peace treaty charges and a stable currency is reestablished, Germany ought in 1926 to be making rapid strides toward complete recovery, and should in three years, by 1928, reach a normal economic condition. We have taken into account the probable yield of her several taxes and her taxable capacity as a whole and the probable changes in expenditure under these improving conditions, and after making full allowance for error we have reached definite conclusions as to the sums which can be fixed for peace treaty charges without endangering the stability of the budget. These results we have considered in relation to the maximum probable rate at which the national income can be expected to grow from its present point and the maximum proportion of

that growth which can successfully be absorbed in taxation.

We draw the conclusion that, allowance being made for some inevitable growth in expenditure, the budgets for the three subsequent years can safely provide for the following maximum sums:

	Gold marks
1926-27	110,000,000
1927-28	500,000,000
1928-29	1,250,000,000

On the other hand, regard being had to the fact that it is difficult to estimate the recuperative power of Germany in 1926-27 and 1927-28, we would propose that these amounts should be regarded as subject to modification by a sum not exceeding 250,000,0000 gold marks on the following plan: If the aggregate controlled revenues as defined in Section XIV exceed 1 milliard in 1926-27 or 1,250,000,000 in 1927-28, an addition shall be made to the above contributions equal to one-third of such excess. Conversely, if those aggregate revenues fall short of 1 milliard in 1926-27 or 1,250,000,000 in 1927-28, the total contributions shall be diminished by an amount equal to one-third of the deficiency.

We believe that at the end of the fiscal year 1928-29 the financial and economic situation of Germany will have returned to a normal state, and that in this and subsequent years the ordinary budget should support the inclusion of a sum of 1,250,000,000 gold marks. The total sums, therefore, to be provided from *ordinary budget resources* would be the standard payment of 1,250,000,000 plus the additional sum (already referred to) computed upon the index of prosperity, as from 1929-30 onward.

We have considered carefully the question of the amount to which the index should be applied and, as we

are desirous that in the earlier years of her recovery German progress shall not be unduly handicapped by shortage of new capital, we think that it will be desirable to apply it to the purely budget contribution, 1,250,000,000 (or one-half of the total standard payment) for the first five years of the application of the index, viz. 1929-30 to 1933-34. After that date, 1934-35, the index should apply on the full amount of the contribution, namely, 2,500,000,000 gold marks.

(b) RAILWAYS

We have conducted, with the assistance of two eminent railway experts, a close examination of the situation of the German railways. The subject is an important one, for the railways have been operated since the Armistice at a constantly increasing loss, which has involved heavy burdens upon the German budget.

Most, if not all, railway systems have passed through a period of great difficulty since the war from causes which were largely beyond their control. It is clear, however, from a study of the report drawn up by the experts, which will be found in Annex 3, that the greatest difficulties were of the Germans' own making. The German railway administration can not but plead guilty to two serious charges. In the first place, as is proved by the reduction which it is now possible to make, they have been enormously overstaffed, even when all account is taken of the introduction of an eight-hour day and of peace-treaty charges justifying temporary disorganization. In the second place, the administration has indulged in extravagant capital expenditure for which the official excuse is that construction was largely undertaken to ward off unemployment.

It is only just to observe that the situation has now improved out of recognition, though more remains to be

done. The German Government has separated the railways from the ordinary administration and assimilated them in form, so far as is possible, to a business concern. Capital construction has been slackened and fares have at any rate been raised to a point where the railways are not only self-supporting but can provide some profit.

These measures are, however, insufficient. The capital value of the railways is estimated by the experts on a conservative basis at 26 milliards. They are unencumbered with old debts, for their prior charges were extinguished by the depreciation of the mark, and these prior charges absorbed half the gross profits in the pre-war period, which amounted to approximately 1 milliard gold marks, in spite of the fact that it was the custom to include in operating and maintenance charges large expenditures which might properly have been charged to capital account.

The railway experts are convinced, and we share their conviction, that under proper management, under unified control, and with a proper tariff policy, the railways can without difficulty earn a fair return upon their present capital value.

Nor need it be thought that this improvement in profits will be made at the expense of the German people by increasing their fares and the cost of all goods transported by rail. It can be substantially provided by the more economical administration of the railways themselves.

In saying this we have not in mind adequate wages, but rather the elimination from operating and maintenance charges of certain elements of waste and also expenditure more properly chargeable to capital account.

The railway experts arrived, however, with considerable reluctance at the conclusion that it would be useless to expect anything approaching the full measure of improvement which is possible, so long as the railways remain in

the control of the Government. The whole spirit of the Government's ownership in the past has been directed to running the railways primarily in the interest of German industry, and only secondarily as a revenue-producing concern, and in their opinion a complete break with old traditions is essential.

We accept their conclusions and we recommend the conversion of the German railways into a joint stock company. It is not our intention thus to deprive Germany of the administration of her railways in favor of the Allies; on the contrary, our plan demands only a modest return on the capital cost, and so long as this return is forthcoming we do not anticipate any interference in the German management of the undertaking.

We would add that if, as the German Government has itself proposed, the exploitation of the railways is divided into several systems, this division should not affect detrimentally their financial unity.

The details of our proposals will be found in Annex 4, and we will content ourselves with giving only a broad outline at this point.

The committee recommends that there should be paid from the German railways 11 milliard gold marks to be presented by first mortgage bonds bearing 5 per cent interest and 1 per cent sinking fund per annum. The capital cost of the German railways computed on a gold mark basis is estimated by our experts at 26 milliards. The net earnings of these railways before the war, after liberal and indeed exaggerated charges to operating and maintenance, were as high as 1 milliard. The interest and sinking fund on these debentures represents less than 3 per cent of the capital cost, which is a very modest charge on the capital investment compared with that required in many other countries of the world.

Realizing that during the period of reorganization of

the railways, full interest and sinking fund charges should not be required, we think payments on account of interest should be as follows:

	Gold marks
1924-25	330,000,000
1925-26	465,000,000
1926-27	550,000,000
1927-28 and thereafter	660,000,000

This is regarded as a normal year.

In addition to the 11 milliards of bonds, the new railway company is to have a capital of 2 milliards of preference shares and the remainder of its capital cost, namely 13 milliards, is to be represented by common stock; 1½ milliards of preference shares are to be set aside in the treasury of the company, for sale to private persons to provide funds for the payment of existing indebtedness and future capital expenditures. The proceeds of the sale of the other 500,000,000 of preference shares and all of the common shares are to go to the German Government.

The railways are to be managed by a board of 18 directors of whom 9 will be chosen by the German Government and the private holders of preference shares, and the other 9 will be named by the trustee of the bonds, 5 of whom may be German. It is therefore contemplated that the board will have 14 German members. The chairman of the board and the general manager of the railways will be German.

It is contemplated that the railway company will be free to conduct its business in such manner as it may think proper, provided always, however, that the German Government will have such control over its tariffs and service as may be necessary to prevent discrimination and to protect the public. Such government control, however, is never to be exercised so as to impair the ability of the

railway company to earn a fair and reasonable return on its capital cost.

The railway commissioner represents the interests of the bondholders. His principal duty will be, in the absence of default in interest, to receive reports, statistical and financial returns, and generally to see that the interests of the bondholders are not menaced.

(c) INDUSTRIAL DEBENTURES

The committee has been impressed with the fairness and desirability of requiring as a contribution to reparation payments from German industry, a sum of not less than 5 milliards of gold marks, to be represented by first-mortgage bonds bearing 5 per cent interest and 1 per cent sinking fund per annum. This amount of bonds is less than the total debt of industrial undertakings in Germany before the war. Such indebtedness has for the most part been discharged by nominal payments in depreciated currency, or practically extinguished. In addition the industrial concerns have profited in many ways through the depreciated currency, such as the long delayed payment of taxes, by subsidies granted and advances made by the German Government, and by depreciation of emergency money which they have issued. On the other hand it is incontestably true that there have also in many instances resulted losses, through the depreciation of currency, from the sale of output at fixed prices, and in other ways.

It is unnecessary for the committee to make an estimate of the total amount of such profits and losses; it is sufficient to say that the committee is satisfied that a burden of mortgage debt of the amount of 5 milliard gold marks on the industries of Germany, fairly apportioned, bearing a moderate rate of interest, and payable on long

maturity, does not create a burden greater than that which would have existed had there been no depreciation of currency.

In fact the fairness of such a proposal has been recognized by the German Government itself in a proposal submitted on June 7, 1923, to all the allied and associated governments.

This proposal was later confirmed by persons in high authority in the subsequent and present German Governments.

The offer referred to above was of 10 milliard gold marks, covering business, industry, banking, trade, traffic and agriculture. The request of the committee is for 5 milliards only and it suggests the exemption of agriculture from the obligation of the mortgage.

Realizing the importance of agriculture to a nation unable to provide its entire food supply, we feel more reserved in making a recommendation as to the burdens which should fairly be put on it, though we can not close our eyes to the fact that a very large amount of agricultural indebtedness has been discharged at merely nominal figures and the owners of equity in land have realized substantial profits at the expense of their former creditors.

We desire to make it clear that the committee in asking for mortgage bonds on industries does not recommend in any sense an unfair or discriminating burden against them, and so we do recommend that equalization be properly and fairly made by the German Government for the benefit of its own budget. If, in the opinion of the German Government, a burden on other property should be imposed in order to equalize the burden of reparation payments on property other than industrial property, we recommend that it be done in favor of the German budget either by a further valorization tax or by a specific lien or otherwise. If this course be followed and

a fair and accurate system of direct taxation be adopted the committee believes that all classes in Germany will be called upon to make their fair and reasonable contribution to peace treaty charges either through direct or indirect taxation.

Realizing the depletion of the liquid capital supply in Germany, and that a period should be provided for its recuperation, we recommend that the interest on the 5 milliards of debentures above referred to be waived entirely during the first year; that the interest during the second year be 2½ per cent; during the third year 5 per cent; and thereafter 5 per cent plus 1 per cent sinking fund. In the event of default in the payment of interest, sinking fund, or principal on any of the said debentures, provision has been made for recovery from the German Government through the commissioner of controlled revenues.

The plan will be found in Annex 5.

X. Summary of Provision for Treaty Payments

We are now in a position to summarize the full provision we contemplate for treaty payments:

Budget moratorium period—

	Gold marks
First year. From foreign loan and part interest (200,000,000) on railway bonds	1,000,000,000
Second year. From interest on railway bonds (including 130,000,000 balance from first year) and interest on industrial debentures and budget contribution, including sale of railway shares	1,220,000,000

Transition period—	
Third year. From interest on railway bonds and industrial debentures, from transport tax and from budget (subject to contingent addition or reduction not exceeding 250,000,000 gold marks)	1,200,000,000
Fourth year. From interest on railway bonds and industrial debentures, from transport tax and from budget (subject to contingent addition or reduction not exceeding 250,000,000 gold marks)	1,750,000,000
Standard year—	
Fifth year. From interest on railway bonds and industrial debentures, from transport tax and from budget	2,500,000,000

The first year will begin to run from the date when the plan shall have been accepted and made effective.

We must point out that the total figures indicated for each year must include the sums paid by the German budget, the railway company, or the debtors on industrial debentures, whoever may be the actual recipients of these sums, the Reparation Commission, the capitalists who purchased securities, or even the debtors themselves if they have repurchased their bonds.

These figures clearly do not include the proceeds from the sale of capital assets which may be effected by the creditor governments. As soon as the plan is put into execution, the Reparation Commission will be in possession of bonds for 16 milliard marks, which may be sold to the extent to which the financial markets are capable of absorbing them. Subsequently, bonds representing the

transport tax and the contribution from the budget may be issued, and will enable the governments to realize the capital of their claims.

XI. Inclusive Amounts.—Deliveries in Kind

THE INCLUSIVE NATURE OF THE PAYMENT

Before passing from this part of our report we desire to make it quite clear that the sums denoted above in our examination of the successive years comprise all amounts for which Germany may be liable to the allied and associated powers for the costs arising out of the war, including reparation, restitution, all costs of all armies of occupation, clearing-house operations to the extent of those balances which the Reparation Commission decide must legitimately remain a definitive charge on the German Government, commissions of control and supervision, etc. Wherever in any part of this report or its annexes we refer to treaty payments, reparation, amounts payable to the Allies, etc., we use these terms to include all charges payable by Germany to the allied and associated powers for these war costs. They include also special payments such as those due under articles 58, 124, and 125 of the Treaty of Versailles.

The funds to be deposited in the special account in the bank are to be available for the foregoing purposes, notwithstanding anything in this report which may be interpreted to the contrary, though in saying this we are not to be read as prejudicing questions of distribution or questions of priority between the various categories of charges.

We venture to emphasize the fact that from the point of view from which we are called upon to regard the question these obligations of Germany are one, and that any addition to one category of charges can only be made at the expense of another.

The committee have noted the important fact that Germany is not in a position to ascertain her liabilities out of the peace treaty as demands are made upon her from time to time during the year, which can not be calculated beforehand. It appears to us a matter of impossibility for any budget to be scientifically compiled and satisfactorily balanced under such an arrangement, and that, therefore, means should be found to bring this system to an end. The difficulty will be satisfactorily met if Germany's liabilities for any particular year are absolutely limited according to our plan and, as suggested above, made inclusive of all possible charges whether in or outside Germany, including the costs of the administrative controls which are set up by our plan.

DELIVERIES IN KIND

We have given special attention to the question of deliveries in kind; in their financial effects, deliveries in kind are not really distinguishable from cash payments and they can not in the long run exceed the true surplus of German production over consumption available for export without either upsetting the exchange or rendering foreign loans necessary.

Having made this clear, we have to remember that:

1. Deliveries in kind are dealt with in the treaty.

2. They are now an inevitable part of the economic conditions of several of the Allies and can not be wholly removed without considerable dislocation.

3. If the principle is not carried too far, they may represent a stimulus to German productivity and therefore the creation of a greater export surplus.

4. They may help in avoiding such surplus being absorbed by the prior action of private German investment abroad. In this connection, the maintenance of the system

of deliveries in kind, if not carried too far, may act in a manner to keep the transfer as large as possible and to give the Allies priority.

While, therefore, we recognize the necessity for the continuance of deliveries in kind, we think that unless they can be confined to natural products of Germany, such as those specifically dealt with in the treaty (coal, coke, dyestuffs, etc.) and in the second place to exports which do not entail the previous importation into Germany of a large percentage of their value, they tend to be uneconomic in character.

In the first two years of the operation of the plan the available finance is so restricted that there will be an automatic limitation of deliveries, but in the later period the program must be carefully and periodically considered in advance by the Reparation Commission in conjunction with the committee referred to in Section XIII if exchange difficulties are to be avoided.

We refer below to the necessity of expending almost exclusively within Germany the sums available for treaty payments in 1924-25 and 1925-26. In these circumstances, the Allied Governments will doubtless consider whether it is not advisable to continue the system whereby the costs of armies of occupation were a first charge upon the proceeds of deliveries in kind made to the Governments which maintain the armies.

Where we have referred to payments for deliveries in kind in this report we have intended to include therein payments in Germany arising through the operation of the reparation recovery acts.

XII. How the Payments Are To Be Made

All payments for the account of reparations (whether from interest and sinking fund on railways or industrial debentures, the transport tax, or from the budget contri-

bution) will be paid in gold marks or their equivalent in German currency into the bank of issue to the credit of the "Agent for reparation payments." This payment is the definitive act of the German Government in meeting its financial obligations under the plan. It is easier to estimate the burden that Germany's economic and fiscal resources can bear than the amount of her wealth that can be safely transferred abroad, and it is the former and not the latter that has formed the first objective of the committee.

XIII. How the Payments Are To Be Received

The use and withdrawal of the moneys so deposited will be controlled by a committee, consisting of the agent for reparation payments (a coordinating official under the Reparation Commission, whose position and duties are defined later in this report) and five persons skilled in matters relating to foreign exchange and finance, representing five of the allied and associated powers. This committee will regulate the execution of the program for deliveries in kind and the payments under the reparation recovery act, in such a manner as to prevent difficulties arising with the foreign exchange.

They will also control the transfer of cash to the Allies by purchase of foreign exchange and generally so act as to secure the maximum transfers, without bringing about instability of currency. Fuller details as to their functions will be found in Annex 6. If the payments by Germany on reparation account, in the long run, exceed the sums that can be thus transferred by deliveries or by purchase of foreign currencies, they will of course begin to accumulate in the bank. Up to a certain point, in normal circumstances not exceeding two milliards, these accumulations will form part of the short money operations of the bank.

Beyond this point, the committee will find employment for such funds in bonds or loans in Germany under the conditions laid down in the annex, but, for economic and political reasons, an unlimited accumulation in this form is not contemplated. We recommend that a limit of five milliards be placed upon all funds accumulating in the hands of the reparation creditors in Germany. If this limit is reached, the contributions from the budget are to be reduced below the standards set out in our plan, so that they are not in excess of the withdrawals from the account and the accumulation is not further increased. In this contingency, the payments by Germany out of the budget and the transport tax would be reduced until such time as the transfers to the Allies can be increased and the accumulation be reduced below the limit named.

We do not deny that this part of our proposal will present difficulties of a novel character which can only be solved by experience. But what are the alternatives?

In order that no difficulties with exchange or stability can possibly arise, the sum payable for reparation may be definitely fixed at such a figure as is certain beyond all doubt to be within Germany's capacity to export in excess of her imports. In this case the attainment of such certainty would involve so low a figure as to be quite unacceptable to her creditors and unwarrantably favorable to Germany.

On the other hand, the liability may be fixed without regard to that excess of exports at all, and the discharge of the liability left to uncontrolled events without any possible regard to exchange difficulties. That way lies future instability and disaster.

We are convinced that some kind of coordinated policy, with continuous expert administration in regard to the exchange, lies at the root of the reparation problem and is essential to any practicable scheme in obtaining the

maximum sums from Germany for the benefit of the Allies.

XIV. Guarantees in Addition to Railway and Industrial Bonds

It is plainly not enough to demonstrate the feasibility of raising the sums under consideration. It is desirable, in the common interest, that means should be devised for securing that the possible surplus is actually established. The greater the extent to which payment may be rendered automatic and a matter of habit and independent of fluctuating political attitude toward reparation, the less will be the friction and the greater will be the real stability of the German budget. In the last resort the best security is the interest of the German Government and people to accept in good faith a burden which the world is satisfied to be within their capacity, and to liquidate as speedily as possible a burden which is and should be onerous.

Creditors, however, are not usually satisfied with a moral security, and experience and the present condition of Germany's finances are such as to reinforce their natural desire for tangible and productive guarantees.

These are no less vital in the interest of Germany herself, who will be relieved of a large part of her political troubles if the main source of political controversy is removed by a system which no longer makes the payment of reparation depend upon the constant maintenance or renewal of governmental decisions. In particular, it is vital in the interests of our scheme, which depends for its success on the assured belief of the whole world in the regular observance of a settlement once made.

On the other hand, we do not hesitate to reject as undesirable, for the purpose which all have in view, save in certain extreme events, any system which would involve

directly or indirectly the virtual control of all Germany's revenue and expenditure. It would involve the controlling authority in responsibility for all financial troubles, and it might be a pretext for them.

The use of this safeguard general budgetary control should be reserved for the case of Germany's willful failure to meet the obligations now laid upon her.

If, as we believe, the payments which we have suggested can be made without compromising budget stability, it is in our opinion not impossible to establish a system under which a combination of self-interest and latent pressure will suffice to assure sound financial administration. We believe that the object can be attained if, without in any way impairing the first charge which now exists in favor of reparation on all Germany's assets, certain specific revenues are assigned to, and under the control of, Germany's creditors. These revenues will furnish a collateral, but not a primary, security and we suggest that they should be the taxes on customs, alcohol, tobacco, beer, and sugar. We propose for this purpose that they should pass directly into the hands of an impartial and effective control; that the treaty payments should first be deducted by the controlling authority for the account of the Allies; and that Germany should only have the use for her own purposes of such balances as may remain.

We believe that this system contains the greatest degree of effectiveness without involving the Allies in the onus of responsibility for any breakdown in the execution of the plan.

We recommend that the control should be instituted forthwith in spite of the fact that the budget supports no peace treaty charge in the year 1924-25.

We make this recommendation for two reasons: Germany, by instituting this control, puts this part of the plan into execution in a definite and public manner, and

in the second place early action will insure that control is in effective operation at the moment when part of the revenues are retained by Germany's creditors.

We would add that while leaving untouched the existing alcohol monopoly, we do not, in view of reports received from technical experts, propose the transformation of consumption duties into new monopolies, though we recommend certain important new regulations with regard to the sale of tobacco.

CONTROLLED REVENUES—THEIR YIELD

The estimate made by the German officials of these revenues for the year 1928-29, exclusive of customs, was 1,700,000,000 gold marks.

The technical advisers specially consulted by the committee have estimated the yield at 2,146,000,000 gold marks.

There is every prospect, therefore, that the assigned and controlled revenues will give a large margin over the treaty charge payments, even in the standard year, of 1,250,000,000 gold marks. The revenues are a security for a payment otherwise fixed. This principle renders possible a system of control which, while equally effective, is much more simple in operation, and is strengthened by the association of Germany's self-interest. Once the treaty charges are met she is entitled to the whole balance and therefore she has the fullest inducement to increase the yield. But she can touch no part of the revenues in a given period until the treaty charges are fully met; so that every increase operates in the first instance to increase the Allies' security.

We have suggested above that in the years 1926-27 and 1927-28 the amount of reparation to be paid should be dependent to some extent on the yield of these particular revenues. In order that there may be no misunderstand-

ing, we desire to state clearly that in our opinion this arrangement should be strictly confined to the two years in question and be regarded as exceptional.

We believe it to be of the greatest importance that the revenues should normally be regarded strictly as security, and should not be relied upon in the ordinary course as the determinant of the actual sum to be paid as reparation. In particular, if the yield of the revenues exceeds the amount to be secured, the excess should accrue to the German Government. Our reasons for holding these opinions are more fully stated in Part II.

XV. External Loan—Its Conditions and Purpose

An integral part of our scheme is the issue by Germany of a foreign loan of 800,000,000 gold marks; this loan is primarily essential for the successful establishment of the new bank and to ensure the stabilization of the currency. The deposit of this amount in the new bank will be an important and necessary contribution to its gold reserves and enlarge the basis of its currency issues. It will thus be enabled in the second place, without impairing its usefulness for the above, to play an important part in solving the problem created by Germany's immediate and more urgent obligations to the Allies which do not necessitate the transfer of money abroad.

We have already stated our conclusion that Germany should not be called upon in the years 1924-25 and 1925-26 to provide for any treaty charges out of ordinary budget resources, and we have deferred to this point indication of means by which a complete suspension of payments may be avoided.

The current liabilities of Germany under the treaty other than liabilities for cash payments in foreign currencies, comprising the most essential deliveries in kind, and costs under a number of other heads, are known to be

considerable. Although their precise amount is not easily determinable, they aggregate to a large amount and if no arrangement is made for meeting or reducing them they form a formidable obstacle in the way of a complete solution.

In the year 1924-25, the extra-budgetary resources can be relied upon to provide 200,000,000 gold marks, being interest on railway bonds. The question arises whether a further sum can be provided.

We first considered whether Germany would have sufficient credit at the outset to meet the full amount of her charges by loans or capital assets. In our view, it is impossible to say that she could obtain funds, until her position is well established, adequate to discharge them. But it does not follow that the most pressing of the demands can not be met, for a considerable sum can certainly be raised upon the good security that the plan provides, with a clear prospect of improved international political position and of stability. The question is, therefore, whether the claims upon Germany can be so reduced by agreement among the Allied creditors as to come within this potential credit. If they can, then obviously the greater the reduction, the more moderate the sum to be raised and the greater the probability of Germany successfully raising a loan. If not, then the loan will not be forthcoming, stability can not be insured, and neither this plan nor any other can come into being. The successful launching of the scheme depends therefore upon three main factors:

(*a*) Limitation of payments for all purposes, to 1,000,000,000 gold marks of which at least 800,000,000 must be spent in Germany for the first year, and thereafter to such sums as are available under the plan during the succeeding years;

(*b*) Cooperation between the Allies and Germany in

securing political conditions which will incline the investors of the world favorably toward the German loan upon good security; and

(c) A loan of 800,000,000 gold marks which will serve the double purpose of assuring currency stability and financing essential deliveries in kind during the preliminary period of economic rehabilitation.

It will be seen that under the plan, among the different revenues available, ample and sufficient security could be found to form the basis of such a loan, both as to interest and sinking fund.

Obviously, the first loan should be fully secured, but it is equally true, that it is neither in the interest of a first loan nor of the Reparation Commission to create a situation which would prejudice the flotation of subsequent German loans or the realization of the capital assets provided for in the plan.

The amount required for the service of this first and any subsequent loans must be deducted from the sums which in subsequent years can, in accordance with our plan, be placed at the disposal of Germany's creditors. In effect the loan is only an anticipation of the sums subsequently available which, it is necessary to emphasize, represent in our opinion the maximum burden and therefore one not capable of increase.

It is not for us to offer suggestions as to the priority of claims or how the sums should be distributed. On this aspect of the matter we confine ourselves to stating that in the interest of currency stability and to aid the successful inauguration of the new bank, the proceeds of the loan should be used exclusively for financing internal payments, such as deliveries in kind (whether direct or by the operation of the reparation recovery act), and that part of the costs of the armies of occupation which represents expenditure in Germany by or on behalf of these

armies. But we do assert that, if as we believe, Germany's credit will be good enough to float such a loan, it is natural and necessary that her credit should be employed to ease the burden on her creditors during the period of her own recovery.

In the year 1925-26, the problem is somewhat different in character. The reasons which make a foreign loan essential in the first year should have disappeared. If confidence is in process of reestablishment a large reflux of capital to Germany is to be expected. People, whose object in transferring money abroad or in hoarding foreign notes within Germany has been simply to insure against further loss, will, to a great extent, reconvert this capital into German currency. Other things being equal, the German currency and exchange situation will continue to improve, a phenomenon which has been clearly exhibited in the last 12 months in Austria.

The exchange position of Germany will, therefore, be relatively strong and her budget position relatively weak. In the few succeeding years the position will be exactly reversed; the exchange will become normal, but weaker than during the abnormal period of reconstruction, while budget resources should be enormously strengthened.

In view of these facts, we see no danger, and perhaps positive advantage, in requiring that during 1925-26 deliveries in kind and that part of the costs of the armies of occupation spent in Germany by or on behalf of the armies should be financed up to 1,220,000,000 gold marks by sums raised in Germany itself.

The above sum is made up of (1) railway interest, partly carried over from the first year, amounting to 595,000,000 gold marks; (2) the transport tax to the amount of 250,000,000 gold marks; (3) interest on industrial debentures amounting to 125,000,000 gold marks; and (4) 250,000,000 gold marks from the budget provided by

the sale of railway preference shares belonging to the German Government. If for any reason the whole of the above sums are not provided, the balance should be raised by a German internal loan.

XVI. Organization

The committee's plan provides for a commissioner of the bank of issue, a commissioner of railways, a commissioner of controlled revenues, the last-named to have under his control a certain number of sub-commissioners severally entrusted with the special revenues under consideration and if the need arise for a commissioner of industrial debenture.

The plan also provides for an agent for reparation payments.

In order that the machinery thus set up by our plan may function properly, both in relation to the Reparation Commission and in its German environments, there must be an agency between the Reparation Commission and the various commissioners. We suggest that this coordinating agency devolve upon the agent for reparation payments.

The commissioners would retain all responsibility for the carrying out of the task entrusted to each, only subject to such coordinating policies as may prove necessary in order to avoid any duplication of effort, overlapping of functions, unnecessary friction and generally all interference with the harmonious working of our plan.

In case of a difference of opinion between one commissioner and the "Agent General for Reparation Payments" in his capacity as coordinator, the commissioner can appeal to the Reparation Commission. The existence of this right of appeal will have a salutary effect upon the relations of the coordinating agency and the different commissioners.

To facilitate the interchange of information which will develop a situation in its entirety for appropriate action a general coordinating board is also suggested in which the various commissioners of representatives named by them will participate together with the "Agent for Reparation Payments" and the trustee. The coordinating board is to have advisory powers only and is for the purpose of giving information to the agent general to assist him in preparing coordinating orders.

These suggestions are naturally far from exhausting this important subject, one of the most important of our plan. They are laid down simply as an indication, as the drafting of the rules for such a coordinating will devolve upon the Reparation Commission so far as they have power, and upon the various Governments.

Rules should be laid down for the rendering of periodical reports and for the publication of such as the public interest may require.

We desire however to record in this connection that the expense of the new machinery provided for by the plan can and should be contained within limited amounts and in any case be included in the annuities already contemplated.

Trustee. The plan also provides for the appointment of a Trustee with the following duties:

He will receive and administer the railway and industrial bonds and will be accountable to the Reparation Commission for these and all other securities.

He will ensure the service (interest and amortisation) of the railway and industrial bonds by means of funds remitted to him for this purpose by the agent for reparation payments.

He will fix the conditions of the amortisation of the bonds and if necessary the redemption at par of all or a part of the bonds not yet amortised, by means of any sup-

plementary payments which may be made by the German Government, the railway company or industry.

With the authorization of the Reparation Commission and for its benefit, the trustee may sell the bonds which he holds, and may use the mortgage bonds and deeds which he holds to secure new securities which he may himself issue.

Both the agent and the trustee should be appointed by the Reparation Commission.

In framing the organization of control, the committee has adopted as fundamental the principle that, if the plan is to yield the best financial results, it is desirable that control should be of such a nature as not to involve the assumption of responsibility by the commissioner for German administration, though the committee recognizes that this principle can not be adhered to in case default under the plan arises.

VXII. The Nature of the Plan

In concluding this part of our report, there are several points which we desire to emphasize.

In the first place we regard our report as an indivisible whole. It is not possible in our opinion, to achieve any success by selecting certain of our recommendations for adoption and rejecting the others, and we would desire to accept no responsibility for the results of such a procedure nor for undue delay in giving execution to our plan.

In the second place, as we have remarked earlier, our plan is strictly dependent upon the restoration of Germany's economic sovereignty, and it is important to observe that the operation of the plan will be proportionately postponed if there is a delay in effecting that restoration. The various dates which we mention in the report must be interpreted in the light of the above remark.

From the standpoint of the taxpayer in creditor countries the plan means in due course an annual relief to the extent of 2½ milliards, plus such additional amount as the index of prosperity may provide.

On the other hand from the standpoint of the taxpayer in Germany the plan means a direct burden of only one-half this sum, viz, 1¼ milliards per year, and the transport tax, plus such additional amount as may represent only a relatively small share in increased prosperity. The German taxpayer can look without anxiety upon the remainder of the payment of 2½ milliards, for it represents a relatively small burden on German industry, which has been the beneficiary of substantial special profits and only a modest return on a large capital invested in railroads which are yielding him no relief in taxation in his budget at present, such capital having been accumulated prior to the war. We are satisfied that the contributions from railway and industrial debentures will not be reflected to any substantial degree in a burden to the individual German taxpayer; as regards the railways it will only require the same kind of return as exists in similar enterprises in many countries.

Our purpose has been to set up a machinery which will secure the maximum payment which Germany can make in each year in her own currency. We do not speculate on the amount which can annually be paid in foreign currency or on Germany's capacity to make a total payment.

The committee is confident that it lies within the power of the German people to respond to the burdens imposed by the plan, without impairing a standard of living comparable to that of the Allied countries and their neighbors in Europe, who are likewise subject to heavy burdens, largely resulting from the catastrophe of the war.

We have not concealed from ourselves the fact that the reconstruction of Germany is not an end in itself. It is only part of the larger problem of the reconstruction of Europe.

We would point out finally that while our plan does not, as it could not properly, attempt a solution of the whole reparation problem, it foreshadows a settlement extending in its application for a sufficient time to restore confidence, and at the same time is so framed as to facilitate a final and comprehensive agreement as to all the problems of reparation and connected questions as soon as circumstances make this possible.

PART II

I. The Currency Position

The conditions at the outset of our inquiry.—When we started our investigations the value of German currency had been stable for some two months. It would not have been pretended, however, by any authority that German currency had been stabilized. It would perhaps be juster to apply the term "unstable equilibrium" than the term "stability" to this transition period, which has fortunately continued to the present day. The elements of permanent stability, even if the repercussions of the budget situation are momentarily left out of account, were then and are still wanting.

One of the first steps which the committee took was to request Doctor Schacht, the governor of the Reichsbank and the currency commissioner of the Reich, to give evidence before them with a view to their being fully informed of the existing currency situation.

Quantity of currency.—The total circulation, although so enormous in nominal values, was, when reduced to its gold equivalent at that date, something over 3 milliard gold marks only, whereas the pre-war circulation in Germany had amounted to 6 milliard gold marks. Prima facie, therefore, the amount of currency seemed deficient rather than excessive, and not likely in itself to be a cause of further depreciation. In proportion as the German mark dwindled in value and became less and less utilizable for the threefold function of standard of value, instrument of payment and medium of saving, foreign

currencies naturally became by force of circumstances, more and more sought after in Germany. The Germans resorted increasingly to the currencies of countries with a comparatively stable exchange, not only to invest their savings, but also to define and even settle their transactions, and the presence of such currencies in Germany increased ever more as the mark depreciated further.

In spite of this extended use of foreign currencies in Germany, the shortage of purchasing power made itself increasingly felt, leading first the German Government, then the States and municipalities, and finally the great industrial and agricultural organizations and even private firms to supplement the currency shortage by new instruments of payment. These token currencies, expressed in gold or paper marks, sprang up in Germany in the summer of 1922, at a moment when the need became urgent to find new means to meet the requirements of current transactions, the old mark on the verge of its collapse no longer answering such requirements.

At the end of 1923, we find in Germany an absolutely heterogeneous monetary circulation, which included besides the foreign money in circulation or hoarded (dollars, pounds, florins, gulden, Swiss francs, French francs, Scandinavian crowns, etc.—the old paper marks, dollar treasury bonds (Dollarschatsanweisungen), bonds of the gold loan (Wertbestandige Anleihe), 6 per cent Treasury bonds (6 per cent Schatzanweisugen), rentenmarks, and, lastly, a whole set of odd emergency currencies (Notgeld) expressed either in gold or in paper marks.

Backing.—The security of the rentenmarks is a mortgage on real and to some extent on personal property. The so-called gold loan is repayable in legal tender on a gold basis but has no gold backing. The various forms of emergency money were for the most part based on no security at all. The gold reserve of the Reichsbank

amounted to some 467,000,000, but 200,000,000 thereof was specifically earmarked as security for the dollar loan issued by the Reich in 1923.

Taken as a whole therefore the liquid backing of the currency is wholly inadequate for a permanent system.

Interchangeability.—The rentenmark is not actually legal currency within the country nor available for any purposes of foreign trade. The old currencies with their vast denominations remain the legal currency, but prices are everywhere expressed in rentenmarks. It is therefore obviously necessary that payments should be made indifferently either in Reichmarks or in rentenmarks at a fixed relation between them. The Reichsbank accordingly accepts rentenmarks at the rate of 1 rentenmark for 1,000,000,000,000 paper marks, and rentenmarks are also accepted in payment of taxes at the same rate.

Annex 7 to the present report shows in some detail the curious monetary situation in Germany at the end of January last.

The present tranquillity.—As the committee have remarked, the elements of currency stability were not to be found in such a situation. The temporary equilibrium of the German exchange has been ascribed to various causes by different authorities; some lay stress upon psychological factors, and in particular a renewal of confidence, the exact basis of which it would be difficult to determine, but which took account of the efforts being made by the German Government to balance its budget, and of the appointment of the Committees of Experts by the Reparation Commission; others refer to a decrease in internal consumption which with the lack of credit, accompanied by what was probably an excessive restriction in importation, reduced the demands both for the circulating medium and for foreign currencies.

Credit facilities.—The exportation of the rentenmark

is prohibited. Its existence was of no assistance in the maintenance of foreign trade. The Reichsmark was too discredited to be any longer available for the purpose of meeting foreign obligations. Credit was only obtainable abroad at dangerously high rates of interest.

At the same time, the currency depreciation and its secondary effect had produced a serious dearth of liquid capital in Germany itself. The stringency may be indicated by the fact that (according to figures furnished us) the savings bank deposits had fallen from 10,700,000,000 at the end of 1913 to 760 gold marks at the end of 1922; the credit accounts in the eight large Berlin banks amounted to 7,400,000,000 at the end of 1913 and to about 1,000,000,000 at the end of 1922. The figures for 1923 are not yet available but can scarcely exhibit an improvement. Leaving for the moment out of account capital which in one form or another had been exported, liquid capital in monetary forms liable to depreciation had been steadily converted into fixed assets with a permanent intrinsic value. The private individual had purchased consumable commodities, while industrial enterprises had largely extended their plant and equipment. The motor was in good, perhaps in unusually good, condition, but the motive power and lubrication were apparently lacking.

Immobile credit resources.—On the other hand, there was general agreement that not inconsiderable resources were available in the shape of German balances abroad and foreign currencies in the pockets of the population in Germany itself. This latter item alone has been estimated at 1.2 milliard gold marks by the committee appointed to consider the means of estimating the amount of German exported capital. It was reasonable to suppose that a large proportion of these resources would be available if complete confidence in the stability of German currency could be restored and maintained.

As stated in Part I, the committee considers that this end can best be secured by the institution under proper safeguards of a new bank which should absorb the existing currencies, liquidate the rentenbank, and transform the Reichsbank, and provide, against recognized banking, cover the foreign currencies necessary for the revival of Germany's languishing trade. The plan for this bank is given in Annex 1.

Psychological considerations seem imperatively to require an institution which should be so far new in its policy and its administration as to detach it entirely from the errors of the recent past and restore the older traditions of German banking.

The interim bank.—While coming to this conclusion and while reducing the general plan to details, the committee had to deal with an actual change in the situation as it originally presented itself. The committee were informed that a scheme for a gold bank was in preparation. It was expressly and admittedly limited to providing the means of carrying on foreign trade. When first submitted it contained some features which the committee would not have recommended, and it omitted others which seemed to the committee to be essential to any permanent settlement of the problem as a whole. Moreover, an attempt to settle particular difficulties in isolation and without reference to other essential requirements appeared to the committee to involve certain risks.

The committee, therefore, without expressing any opinion on the plan as given to them in outline, assured themselves in consultation with the authorities responsible for Germany's monetary policy that the bank would be so organized as to facilitate its absorption into a new bank of issue which might be set up in accordance with the recommendations of the committee.

II. Consideration Regarding the Measurement of Germany's Burden

(a) commensurate taxation

In Part I we refer to the fact that we have taken full account of this principle. But it is necessary for us to make some further observations thereon.

The principle of the "commensurate burden," as it has been called, unimpeachable in abstract statement, is exceedingly difficult to translate into quantitative measurement as a basis for practical action. While obviously sound and just, it does not easily admit of precise and arithmetical calculation. What at first sight seems to be a simple conception, on examination is found to be complex and in some respects not reducible to exact definition.

Now the ordinary expenditure which has to be provided for in the German budget is reduced, in part by the restriction upon her military preparations but above all by the practical extinction of her internal debt.

If Germany had sustained the burden of her own debt, as the Allies have done, and not obliterated it by inflation, she would have had to raise 4½ to 5 milliards per annum in addition to her domestic expenditure.

This would make it both just and practicable to add a provision in her budget which should bear some correspondence to the provision made in the Allies' budget for their war expenditure.

But the raising of any particular sum from one section of her inhabitants, to be paid back to another section within her borders, is a "burden" in a different sense from the payment of such a sum by the whole population to people abroad—different in more than the economic sense—and it is difficult to bring such a task into direct relation with the problem of reparations. It is a measure

of what individual taxpayers, rather than a nation, may be capable of bearing.

In the first case the interest paid forms a part of the national income, as it is expended it provides profits and a stimulus for internal trade and so increases further the income of the country, and in particular it is itself an important source of internal taxation.

A payment in respect of a debt to foreigners has no comparable advantages to the country making it. The extinction of the German debt has after all been at the expense of her own nationals, who are her taxpayers; they have sustained as holders of German bonds, not only the burden which they have already escaped as taxpayers, but that which they would have borne in future years to meet the service of the internal debt if its value had not been destroyed by depreciation. The process of extinction has indeed (except in its incidence as between different individuals and classes) had the same results both to the treasury and to the German taxpayer regarded collectively with a capital levy devoted to debt extinction.

The loss incurred by individual holders of debt is exactly offset by a corresponding profit accruing to the taxpayers as a whole.

It renders both practicable and just a greater charge for other war debts than would otherwise have been possible. A large proportion of the richest taxpayers of the country have obtained the relief without themselves sustaining the cost. They are a proper source of taxation commensurate with that weighing upon the corresponding classes in allied countries and in particular upon the industrial classes. To them as individual taxpayers a tax is a tax whether its ultimate destination is the payment of a war debt due to fellow citizens or to foreigners. And under the system we propose it may be regarded as a tax in internal currency without the complications which re-

sult from the question of how sums so received can be converted into foreign exchange. For this special problem we provide special safeguards. The German taxpayer should regard a payment in respect of war debt exactly as an allied taxpayer regards a similar payment. Its ultimate destination need not concern him, and is certainly no justification for him to attempt to evade it.

The facts as to the burden actually being borne by the Allies for debt service are perhaps a better approach to the actual problem. If the German burden per head for debt were as onerous as the burden for debt existing upon the inhabitants of Belgium, France, Great Britain, and Italy taken together, then the German debt charge would approximate to 6 milliards. But in this case, again, the charge is to a considerable extent in the nature of a redistribution of annual wealth among the members of each nation and has little relation to the problem of a national burden in the collective sense.

In the third place, it may be said that if the German people were burdened as heavily as the members of the most heavily taxed of the allied countries are taxed for all purposes, *excluding debt charge*, we should have an expression of the commensurate burden principle in a limited and strictly defensible sense. But even here theoretical and practical difficulties prevent exactness.

In the search for the "commensurate" it is not enough to compute the burden as a per capita charge, it must be related to per capita wealth or income; it is considered by many that justice requires a "minimum of subsistence" to be first deducted from such per capita income; the amount of the minimum is not exactly determinable and it seems to vary as between different countries of different climates, different economic development, and different customs, e. g., as between Spain and the United States; it may even vary between different

periods in the same country. As a rough working assumption, such a minimum may be regarded as varying in proportion to the per capita income of different countries. Furthermore, over any period of time this burden per head in the allied countries must change and what might be a valid comparison to-day in taxation in those countries may be quite different in 10 years' time. The comparison of statistics of total taxation, national and local, in each country presents many technical difficulties. Moreover, statistics of total national income and income per head are at present either very defective or wholly lacking. Notwithstanding these difficulties it is possible to compute roughly what total budget charge would be borne by the German people if they were subject to taxation (central and local) on the same scale per unit of income as in Great Britain, and by deducting from the result the necessary domestic expenditure to derive an arithmetical balance which could be, theoretically at any rate, assigned to the payment of reparation.

Combining these various aspects, we have reached the view that the "commensurate burden" principle for Germany, when she is fully restored to economic prosperity, would more than justify all the practical conclusions we have set down and that they are in every way morally defensible.

There are, of course, good reasons of a political, economic, and psychological character for confining the actual requirements of budget accumulation within Germany to limits well below the figure that would be arrived at from the consideration of this principle by itself. Different individuals will differ in the degree of importance they assign to such reasons. It is perhaps unnecessary to state these aspects in detail and sufficient to register our united conviction that all our recommendations and suggestions are well within what can be

morally justified on the principle of "commensurate burden," whatever limitations may be placed upon that principle. In this sense, therefore, the justice and moderation of our proposals ought to be fully recognized by the German people themselves.

In the above discussion we have disregarded the question of railway profits. Inasmuch as budget revenue is not derived from profits on railways elsewhere, no question arises as to whether railway profits are a burden (in the sense of a tax). Such profits in other countries form a part of the ordinary profits of private concerns accruing to individuals, and it may be said therefore that in Germany the position of the taxpayer is the same, whether such profits go to individuals or to the Allies as reparation.

On the other hand, the German railway profits might go in relief of taxation burdens if they were not applied to reparations. Moreover, it is difficult to say that the abstraction of the profits of so important an undertaking as the railways of a country from that country, instead of leaving them there to be enjoyed individually or collectively by the inhabitants, is not a "burden" in the international sense, even if it is not a part of the individual *commensurate burden of taxation.*

(b) EXPORT STATISTICS AS AN INDEX OF PROSPERITY

In Part I we have suggested an index of prosperity and indicated that in our opinion it was a fairer test than the existing index, namely, export statistics. The use of the latter in isolation has certain definite defects, to some of which we desire to draw attention.

1. Foreign trade only covers part of the area of total trade, and if foreign trade at a given moment only covers a small part of the area, total trade may be moving in a direction opposed to that of foreign trade.

2. Artificial conditions, such as alterations in transport charges, may affect the trade figure in the absence of any real change in the value or volume of exports.

3. The export statistics, more especially when no export duty is in force, may be subject to changes in presentation and frequently furnish material for controversy.

4. Reparation payments themselves are, and can only be, financed by an excess of exports. It follows that an increased reparation payment in one year furnishes an increased base for the following year. This process is cumulative, and the basis for the index is continuously raised, so to speak, at compound interest, even though actual prosperity may be stationary.

5. In a country with an economic life such as that of Germany invisible exports may increase more rapidly than physical exports, and there may be a growing prosperity which is not reflected in export statistics.

(c) MEASUREMENT BY YIELD OF PARTICULAR TAXES

We have laid some stress in Part I on the fact that certain revenues were chosen strictly as guarantees and that fluctuations in their yield were not to be regarded (save in 1926-27 and 1927-28 exceptionally) as determining the payments due by Germany. The following are the broad principles justifying this standpoint:

1. It is desirable that the German Government and the German people should be themselves interested in increasing the yield of the controlled revenues, and should be under no temptation to discriminate against these taxes in favor of others.

2. The year's liability, which under our plan includes an allowance for increased prosperity, will already have been established by one test, in which, moreover, the yield of the controlled revenues indirectly forms one element.

Having applied one test, it would be unfair to apply a second and to choose whichever gives the higher result.

3. The year's liability ought not to vary with the fortuitous yield of particular taxes. The character and level of these taxes should be chosen with a view to their suitability as security and not with a view to their appropriateness for fixing obligations.

Unless the liability of the year is definitely fixed and unless the German Government can proceed to estimate its resources by reference to the whole and not part of the taxable field, the difficulties of forming a satisfactory budget are aggravated and German credit is affected.

4. Common sense requires that the reparation liabilities ought not to rest even indirectly upon the rate of particular taxes, or otherwise every change in rates or methods of collection, even when thoroughly justified by social or political reasons, must be scrutinized with such a degree of care and perhaps suspicion that it becomes a fruitful source of friction and dispute.

III. The German Budget for 1924-25, and the Fiscal System

The 1924-25 budget.—The German Government prepared and submitted to us the outline of a provisional budget for 1924-25 which estimates a small excess of receipts over the ordinary administrative charges of the country. (Annex 8.)

While the committee have spent a great deal of time upon the details of this budget, and have put many questions in writing to the government and in oral cross-examination of the officials upon its chief features, the subject is so vast in its ultimate implications, especially having regard to the constitution of the Reich, that no finality could possibly be reached, especially in a matter which to the Germans themselves is full of difficulty and doubt. Nevertheless, we believe that the ground

has been explored to a sufficient extent to justify us in feeling that even a prolonged examination could not substantially alter our conclusions. To some of the more salient points we shall make particular reference.

The conditions under which the budget estimates were made.—It should, however, be first remarked that in general the budget must necessarily be in the nature of an experiment and the individual items in it somewhat arbitrary estimates. At the time of our investigation Germany was passing through an acute economic crisis, the direct result and the culminating point of a depreciation of the currency so catastrophic as practically to destroy the currency and reduce the budget to all but a shadow. The habit of saving has been destroyed, and it will require time and the restoration of confidence to reestablish it. The existing wealth is maldistributed in an almost unparalleled degree. The cessation of depreciation, with the consequent removal of the premium on export and the stabilization of prices at a level which is momentarily at any rate above that of the world level, has had important reactions. Finally, the state of employment and the fiscal and economic machinery of Germany have been violently deranged by the events of 1923; a return to normal conditions in this respect can not be effected overnight.

Assumption underlying the budget.—It should be most carefully noted that the budget is not made up to represent the financial expectations of actual existing conditions. As we have remarked above, the general budget as presented anticipates a credit balance, and the German Finance Minister appeared to be reasonably confident of his ability to live up to these estimates, provided three essential conditions were fulfilled:

1. That the bank of issue which would serve as a basis for the grant of credits would be established.

2. That the full development of German economic life should not be restricted by the severance of the Ruhr and the Rhineland.

3. That Germany enjoyed complete freedom in her economic relations with other countries.

The first and second of these conditions will be fulfilled if our recommendations are accepted, and they appear to us to be essential to budget equilibrium. As regards the third, we understand that Germany's commercial freedom is restored under the terms of the treaty in less than 12 months' time.

We are not, however, satisfied that the budget as framed is not exposed to a real risk of deficit. The German fiscal year begins on the 1st of April and even if our recommendations are accepted a certain lapse of time will be necessary before an absolutely normal administrative situation can be reestablished.

For this, if for no other reason, we conclude that on the existing basis of taxation the estimated revenue may not be realized, even allowing for certain possible underestimates under particular headings.

On the expenditure side, the only item on which a saving may emerge of any great significance relatively to the possible deficit is the provision of relief for unemployed. The sum allocated to this purpose (500,000,000 gold marks) is estimated on the assumption that the existing amount of unemployment will continue throughout the year. It appears to us that this is unduly pessimistic and any reduction in the number will both relieve the expenditure and the revenue side of the budget, inasmuch as the wages earned by a laborer are subject to direct, and through the medium of his expenditure, to indirect, taxation.

Taking one item with another, however, we can not justifiably state that the results are likely to be any

better than have been indicated in their estimate. But if, for this year 1924, there was a deficit (we have just seen that this possibility can not be absolutely disregarded) we can assert that it would not be of an extent to endanger the stability of the currency, or force the German Government to have recourse to other than the conventionally authorized expedients for meeting it, such as increases of existing taxation, further emergency taxes, or small internal loans.

Moreover, so many of the settlements due in the year 1924 will fall to be made in the year 1925-26, that fiscally these two years tend to be merged into one period, and, as will be seen later, we have no doubt that in that period ordinary budget receipts will fully equal ordinary budget expenditure.

Special features in the fiscal system.—The Income Tax.—We do not propose to comment in any detail on the existing taxes, but there are certain broad features which call for notice.

We have been unable to escape the conclusion that the wealthier classes of Germany have, in recent years not been reached properly by the system of taxation in force, either to an extent which the taxation of the working classes would justify, or to an extent comparable with the burden upon the wealthier classes in other countries.

It is, of course, common knowledge that, with a continually depreciating currency, many classes of business men tend to obtain as profit a larger share than is normal of the total produce of industry. Many of their expenses are in the nature of fixed charges; moreover, generally speaking, paper-mark wages have not advanced as rapidly as paper-mark prices have increased, so that the share of the business proprietor in the total produce of industry, altogether apart from the special profits made by him on

redeeming debentures or mortgages at nominal figures, has tended to be greater than is normal.

Direct taxes, such as income tax, are necessarily assessed for completed periods and during a time of rapidly rising prices the burden of any particular year, based on the profits of previous years, is small relatively to the profits of the year itself. Moreover, the process of return, assessment, and appeal for such a tax, necessarily occupies further time and by the date when substantive liability is fixed in paper marks its real burden is far less than was originally intended. Further delay in payment of that liability intensifies this effect. It was not until the inflation movement was well advanced in Germany that any serious effort was made to combat this evil. Although the rates of income tax according to the nominal scales rose to nearly 60 per cent on the highest incomes, statistics of cases furnished to us by the German Government show that in effect, even in the year 1920, the burden of actual tax (measured in gold) on the higher incomes, instead of being 50 to 60 per cent, was only half those rates upon the income of the year (measured in gold). This was undoubtedly one of the primary causes for the budgetary difficulties of Germany, and the disparity was very much greater in the later periods. It can be said with confidence that the wealthier classes have escaped with far less than their proper share of the national burden, and we have put it as a matter for the serious consideration of the German Government whether they should not, facing even the admitted administrative difficulties, review the assessments of recent years in the case of these particular classes of taxpayers and reassess their liability upon a gold basis.

The whole system of direct taxation went to pieces in 1923 and, for 1924, the income tax, as is easily understood, is in abeyance. The profits of industry in 1923 expressed

in nominal figures of paper marks have no meaning unless they can be resolved into the profits of the particular dates on which they were made and then reduced to a common denominator of gold values. A profit of 1,000 marks made in January, 1923, is obviously quite a different amount from 1,000 marks made in September. We can well believe the German Government finds it impossible to use the year 1923 as a basis for income tax assessment in 1924.

They have been driven to temporary expedients of a very makeshift character, not rising to a higher normal burden than 25 per cent, with the intention of rescheming and reassessing the income tax proper in 1925.

These expedients do not reassure us upon the general question as to the taxation of the wealthy classes, and, in our judgment, if they desire the Allies and their own working classes to realize their good faith in this matter, the German Government should publish at an early date their definite intentions with regard to the scales of income taxation that are to be applied during 1925-26 to the actual profits of 1924-25 for the final adjustment of the fiscal year 1924-25.

The 1924-25 budget estimates 1,344,000,000 gold marks as the income tax yield, of which all but 480,000,000 gold marks is estimated to be assessed on wages.

We have drawn the German Government's attention to the absence in the temporary measures of any proper provision at present for dealing with income from abroad. They were asked to furnish us with details of the comparative position of different incomes drawn from dividends in the years 1920-21, 1923-24, and 1924-25. The reply is given in Annex 9 as indicating the present position of direct taxation in Germany.

Special taxation on those who have specially profited by depreciation of currency.—Currency depreciation, on

the scale it has occurred in Germany, has brought into existence a new and special type of "windfall" wealth which is a suitable subject for taxation in an emergency.

The ultimate profit or loss to industry and agriculture as a whole of the depreciation era may be difficult to calculate. There are many cases, however, of industrial and other undertakings which were not only able to make large profits but succeeded in paying off prior charges at a trifling fraction of their value when incurred.

If a mortgage or debenture of 10,000 marks has been paid off for practically nothing, a "windfall" profit to the debtor (at the expense of the impoverished creditor) has been made to that extent. If it has not yet been paid off, but the debt can in due course be discharged by worthless paper marks, the "windfall" is a potential one. In this last case, it has been decided by the German Government to "valorize" the debt at 15 per cent and the windfall to the creditor is to be restricted to 85 per cent. On this remarkable improvement in his position, the Government proposes to levy a tax of 2 per cent, or 1.7 on the whole debt. In the case where the debt has been paid off, the Government will take the actual difference between the gold price paid and 16.7 per cent. In our view, such special taxation, if justified in principle at all, as we believe it to be, is justified at much higher rates. But certain rights of taxation are being given to the Federal States which encroach upon this area of taxation, and, for the rest, our proposals (Section IX *(c)* of Part I) in regard to industrial debentures cover what might otherwise have been independent recommendations under the head of taxation.

Similar extraordinary profits have been made through State subventions and through the repayment in depreciated currency of bank loans, State advances, and other similar obligations.

The Reich and the States.—The third special feature to which we would refer is the financial relation between the Reich and the States and communes.

The more complete financial centralization that took place after the war in accordance with the Weimar constitution has not fundamentally changed the character of the relations between the Reich and the States. Although the Reich is charged with the administration of taxes formerly undertaken by the States, it is under obligation to cede the major part of the proceeds of the income tax, for example, to them. The States discharge wholly or in part many of the functions of government, and there is no clear principle connecting their resources with their obligations. When in difficulties, they press the Reich for larger subventions (as precentage of the yield of taxation), just as in turn the needy communes press the States for greater financial aid.

The situation has hitherto been governed by merely political or administrative opportunism rather than by clear financial principle. The Reich can either yield to the pressure for higher percentages in subvention or they can confer upon the States the right to exploit particular fields of taxation for themselves. The check by the States upon the communes is equally unsatisfactory. It is almost impossible to ascertain the true cost of any of the single functions of government in view of its division between these three constitutional entities, and in the absence of proper aggregated financial statistics of the States and still more of the communes.

The changes that have taken place completely falsify any comparison which could be established between the pre-war Reich budget and that for 1924-25.

Moreover, these relations are once more under review. During the period of rapid depreciation the resources of the States and communes, together with regular alloca-

tions from the revenues of the Reich, were inadequate to their needs. Their financial situation was similar to that of the Reich itself.

The expedient adopted by the Reich of multiplying the issue of notes was not open to the States and communes, who had necessarily to be supplied with continuously increased subsidies from the Reich, and this proceeding was one of the principal causes of the utter breakdown of the German finances.

The resultant chaos has been such that no up-to-date statistics are available, and the States have not yet framed their budget on a gold basis. It is in our opinion essential that at the earliest possible moment the preparation of complete statistics of the receipts and expenditures of the States and communes should be resumed.

The importance of the question may be seen if it is realized that the Reich budget, after allowing for the subsidies, contains little more than one-third of the total expenditure, one-third being met by the States and one-third by the communes. It would be quite possible for the communal budgets to be enjoying considerable prosperity at the same time that the Reich budget is in serious difficulties.

We do not pretend to be in a position to make detailed recommendations; the subject is a complicated one and involves the consideration of social and political factors, many of which have deep roots in historic traditions.

Moreover, if our recommendations are accepted in their entirety, self-interest alone may almost confidently be relied upon to force the German Government to make provident arrangements with the States, and it has already given us an assurance that the régime of increased subsidies has come to an end and will not be revived.

It is clear, however, that in the near future the German Government must take steps to put the relations

between the Reich and its component parts on a regular basis which shall insure that the latter are not a constant drain upon Federal resources; the existing hole in the budget must be plugged.

It does not suffice, in our judgment, for the Reich to remain in supine contentment with the present situation merely because it has been the result of constitutional evolution. Germany waged war as an undivided whole and the financial responsibility of the Reich to the Allies can not be qualified or weakened by an attitude of passive acquiescence in the undiminished rights of subordinate areas. So long as Germany has any external obligations they must be paramount, and the resources normally to be assigned to the States and communes must be clearly defined, and care must be taken to secure that these resources are not more than adequate to legitimate needs.

Where further assistance must be given by the Federal Treasury, the amount of such assistance should again be strictly proportioned to the necessities of each case and subordinated to continually increasing central supervision by the Federal Treasury of local expenditure.

In considering the budget as drafted in 1924-25, we have felt compelled to assume that the assignment to the States amounting to 1,800,000,000 gold marks is an irreducible figure, and that if the States themselves have budgeted for the receipt of this sum the Reich will be unable to escape the liability in one form or another. This is the most probable assumption which we can make in a matter which bristles with political difficulties, and it is supported by the estimates submitted to us of the revenue and expenditure in 1924-25 of Prussia, Saxony, and Bavaria; in each case deficits are disclosed.

FURTHER COMMENTS UPON PARTICULAR TAXES

1. The committee recognize that the taxation of each

large nation to-day is the product of many factors, including its historical evolution, its economic conditions, its political ideas, its constitutional framework, and its social psychology. What is a good system for one country may be quite unacceptable for another. Even though the same elements may exist in two systems, the importance played by those several elements in the whole may be quite different. If a similar total burden is being raised in two countries, it is almost certain that the manner in which it is being spread over the community and the particular devices adopted to raise it will be very different.

2. For these and other similar reasons we do not regard it as particularly profitable to pass the German budget in detailed review merely to suggest that each particular tax can be raised to a rate or level found in some allied country for that tax, and thus to impose upon Germany the maximum burden borne under each head in any of the creditor countries. To do this would be to lose sight of the principle we have referred to above, and also to ignore the question of the total burden. For example, to state that Germany could stand increases in the rates on tobacco, beer, spirits, etc., to the level of those in England, while ignoring the existence of her high turnover tax, which England does not impose; or to state that Germany could bear increased rates of death duties, while wholly ignoring the existence of her capital taxes, would be to destroy the balance of her system, and be oblivious to the total burden thus accumulated. The committee would desire to avoid being dogmatic as to the way in which a given sum shall be raised by the German Government. Having come to the conclusion that a given burden can be borne, it is for Germany to suit her own conditions in prescribing the ways in which it shall be obtained. At the same time, diverse as the systems in the allied countries themselves are, the committee offers the following

suggestions as the subject of their common agreement and as suited, in their judgment, to German conditions:

1. *Tobacco*

Eminent technical experts have made the following suggestions, which we commend to the notice of the German Government:*

While they believe that the institution of a tobacco monopoly would entail heavy immediate expenditure, thus causing economic disorder, the technical experts recommend that the free manufacture and sale of tobacco should only be allowed to continue if subject to the regulations of the following scheme:

1. No factory, nor wholesale or retail tobacco shop may in future be established nor may any existing establishment be enlarged without the permission of the State.

2. The introduction of tobacco substitutes in manufacture is prohibited.

3. The number of existing factories must be reduced by abolishing, with a fair indemnity, those which are really not industrial in character, while all factories which have been proved by experience to be incapable of producing goods at a fair cost price must be expropriated.

4. Products manufactured in the various factories shall still be sold with their trade-mark, while the sale price to the consumer shall be indicated on each package; each box or packet to be sealed with a band representing the State guarantees.

5. Existing manufacturers shall form a consortium according to the category of goods produced. This consortium, while collectively undertaking to supply the State with the quantities required for consumption, shall

* These suggestions are contained in a report drawn up by M. Mayer and M. Aliprandi, which will be put at the disposal of the Reparation Commission, together with a report on indirect taxes drawn up by M. Hulin and M. Mazzucchelli.

have to deliver its products at its own expense and exclusively to the State warehouses indicated.

6. The products manufactured shall be bought by the State at a price to be fixed at regular intervals.

7. Prices shall be fixed in conformity with the results obtained in one or two State factories, to be run for experimental purposes and for the control of prices.

8. Importers of foreign manufactured products shall be free to continue their business on the sole condition that they sell the imported products to the State warehouses, under the same conditions of delivery as home manufacturers who deliver the goods produced in their factories.

In regard to sale organization, the technical experts make the following recommendations:

1. The State shall use the wholesale dealers' warehouses for its own purposes.

2. Retail sales must be carried out exclusively by licensed retail dealers.

3. The retail dealers must only sell State products bearing the proper guarantee band at the price fixed on the package.

4. The remuneration of retail dealers shall be fixed at regular intervals by a certain rate of commission on the sale price to the consumer, such rate not to exceed an average of 12 per cent. Bonuses within this limit of 12 per cent would encourage the most energetic retail dealers and thus develop the turnover.

5. Payment for manufactured products delivered to retail dealers shall be made to the warehouse supplying them by means of check or postal order (not in cash and without credit) minus the commission above stated.

6. A small number of State retail shops shall be instituted in order to obtain reliable estimates and to control the expenses of sale.

On the basis of this plan the technical experts make the following estimate of the profit to be obtained by the State:

	Swiss francs
Cost of manufacture	476,160,000
Manufacturer's profit and additional general expenses (35 per cent of the cost of manufacture)	166,656,000
Expenses for the warehouse service and general expenses of the sale organization (1 per cent of the gross receipts)	20,906,400
Cost of delivery to retailers (12 per cent of the gross receipts)	230,876,800
Additional expenses for transport (80,000 tons × average distance of 25 kilometers × 0.25 franc)	500,000
Annuity payment in the event of the indemnification of one-fourth of the present manufacturers	16,975,000
Total expenses	912,074,200
Gross receipts (according to Tables V and VI)	2,090,640,000
Net profit for State	1,178,565,800
That is.....gold marks	856,515,000
Percentage of net profit	56.4

The technical experts have the following observations to make on the above table:

1. An annuity payment is provided for, which would correspond to the amounts to be allowed for the indemnification of the small factories to be closed down.

2. The cost prices of a free industry distributed amongst a large number of factories are higher than those of a monopoly. Consequently the costs of manufacture under a monopoly system are increased by 35 per cent in order to allow the manufacturer a reasonable profit.

3. With this organization, which leaves the factories and retail establishments in their present form, the taxes now collected by the German Government would no longer have to be deducted, with the sole exception of the tax on wholesale dealers to the amount of 6,000,000.

Under a system of sale, organized in conformity with this scheme the technical experts put forward the results of such a plan as under:

	Gold marks
Gross receipts (amount expended by consumers)	1,523,960,000
Profit obtained by the State from which must be deducted the taxes at present collected by the Reich	856,515,000
Customs, tax on turnover	6,000,000
Net profit obtained by the State	850,515,000

The technical experts consider that it would be preferable to entrust the sale organization to an entirely autonomous organization, the constitution of which might well be based on the example of the Swedish monopoly. On the other hand, it is their opinion that the present fiscal organization of the German Reich should be used for the supervision of the tax.

In conclusion, the technical experts believe that during the first period, which would not exceed two years, the estimate of the guaranteed net profit might be based on the assumption that each inhabitant spends only 26 Swiss francs per annum, which is the figure now obtaining in Austria. Such a figure would yield a net profit of 657,000,000 gold marks, on the following estimate.

	Swiss francs
Gross receipts 26 × 62 millions...	1,612,000,000
Total expenditure *	707,917,000
Net profit.....	904,082,000

or 657,000,000 gold marks.

To recapitulate, the guaranteed revenues for the payment of reparation which Germany might obtain by the tobacco tax would be as follows:

	Gold marks
1924-25.....German estimate....	498,000,000
1925-26.....do.....	657,000,000
1926-27.....do.....	657,000,000
1927-28.....do.....	856,000,000

A considerably larger sum can be realized from the German duties, while decreasing the burden falling on the German consumer. The less efficient factories will be eliminated and substitutes will be abolished; surplus profits of the intermediaries will be reduced, leaving them nevertheless a reasonable margin. Without introducing the monopoly reform, standard factories will be instituted (one or two factories to control costs and few selling shops) and the sales will be strictly disciplined.

The proceeds would be paid periodically by the "Service of assigned revenues," either:

(*a*) In the case of the adoption of the "assiette" suggested by the technical experts, on the basis of 60 per cent of the gross revenue (as the technical experts themselves have calculated that 40 per cent represents purchase price of manufactured tobacco, plus cost of distribution, etc., the remaining 60 per cent represents an absolutely net profit from the duty); or

* Expenditure shown in the table on the previous page reduced by 36-33.72 with the exception of the expropriation annuity.

(b) Otherwise, on the basis of a sum in gold marks for every kilogram of tobacco taxed, according to the various chief qualities of the tobacco; this sum to be fixed by the technical experts.

2. *Indirect taxes generally*

The rates appear to the committee to be unduly low, and, as prosperity grows, to be susceptible of increase without diminishing consumption.

3. *Turnover tax*

It is our general opinion that this tax should at the earliest possible moment, be somewhat reduced in favor of other forms of taxation.

4. *Taxes on motor transport*

It is considered that the present total burden is too low and that a substantial further sum might be raised without detriment either by a tax on petrol or a supplementary duty on motor cars, or by a combination of these means.

5. *Death duties*

The yield from these duties is extraordinarily low judged by almost any standard. It is not satisfactorily accounted for by the temporary depreciation in capital values which is due to lack of profits and trade output. Not only is the total yield low judged by any test as to capital values, but the actual rates of duty being imposed are also, in the committee's judgment, inadequate. While not unmindful of the effect of the relation between these duties and the capital tax in general, the committee thinks that the position disclosed in the following table, compiled by the German Government, indicates that there is con-

siderable room for increased taxation under this head. It will be observed that where the rate in Germany is nominally higher than that in other countries, it is in those scales where the tax may be least influential in its effect upon total yield.

Annual taxation on capital, in the committee's judgment, tends to become a part of the income tax system and to discriminate between income derived from work and that derived from investment. In this case, therefore, taxation of capital by annual payments is in a different category from ordinary succession duties.

FISCAL BURDEN CONSTITUTED BY THE DEATH DUTIES IN GERMANY, BELGIUM, GREAT BRITAIN, AND FRANCE

[Burden expressed in percentage]

Property left (in gold marks)*	Germany	Belgium	Great Britain	France
WIFE AND THREE CHILDREN				
20,000	1.5	2.1	3.0	3.5
200,000	2.9	2.7	5.0	6.1
2,000,000	5.9	3.8	15.9	11.5
6,000,000	7.5	4.8	22.8	14.4
BROTHER				
20,000	7.8	8.3	3.0	23.3
200,000	17.4	11.4	5.0	36.0
2,000,000	30.0	17.0	19.2	50.1
6,000,000	30.0	22.2	25.9	56.2
PERSON NEXT OF KIN				
20,000	18.2	16.7	3.0	36.8
200,000	40.6	22.8	5.0	48.3
2,000,000	70.0	34.8	23.5	61.0
6,000,000	70.0	44.5	29.8	66.5

*The foreign currency has been converted into gold marks on the basis of the average rates of exchange quoted for the currency at issue on the Berlin Stock Exchange in the month of January, 1924. According to these quotations 1,000 gold marks were equivalent to—55.5 pounds sterling in round numbers, or 5,000 French francs in round numbers, or 5,550 Belgian francs in round numbers.

IV. Proposal for Control of Revenues Assigned as Security

It is necessary to elaborate in rather fuller detail the recommendations which we have made in Part I of this report for the assignment of the taxes, etc., on tobacco, alcohol, sugar, beer and of the customs revenue as security for payment of the sums charged annually on the German budget.

As regards the year 1926-27, 1927-28, as already indicated, the assigned revenues will play a special part in our plan. They will not only serve as a guarantee to creditors, but also as a means of measuring the contingent addition to, or deduction from, the total amount of reparation payments laid down in the plan. If the yield of these revenues falls short of one milliard in 1926-27 or 1¼ milliards in 1927-28, the reparation payments will be diminished by an amount equal to 1/3 of such deficiency; on the other hand, if they exceed those limits, there will be an additional payment equal to 1/3 of the excess; both deduction and addition however are limited to an amount of 250 million in each year.

In 1928-29, and subsequent years, the amount of Germany's obligation is fixed by the standard payment, plus supplementary payment (and into the computation of the latter, the increased consumption of these taxed articles will enter).

The total yield of the controlled revenues will be paid into the account of the agent for reparation payments as from the time when the plan is put into execution.

In the first year in which there is a charge on the budget and in all subsequent years, the amounts required to meet the charge will be retained and the balance will be periodically released to the German Government.

We propose that there should be one commissioner to supervise the controlled revenues and under him a sub-commissioner for each of the five controlled revenues.

In order that the Reparation Commission may be in a position to secure an officer of the greatest experience and efficiency as chief commissioner, the area of selection should be as wide as possible and not confined to the Allied countries.

He should have the assistance of a consultative and advisory committee on which each of the interested allied countries would be represented.

The various German services of the assigned revenues would be obliged to deposit, through the receiving offices, immediately on receipt, the amount received under the head of the revenues in question at the nearest branch of the central bank acting as treasurer.

A. *Funds.*—The separate branches should pay the sums into the central bank to an account at the disposal of the commissioner, who should afterwards provide for the periodical "reversements" to the German Government of sums in excess of the proportion of the year's peace treaty payments accrued to date.

B. *Audit.*—The commissioner would impose such methods of independent audit as he might desire to ascertain that all assigned revenues:

1. Were properly obtained from the public, and
2. Flowed through the control administration.

C. *Detailed responsibility for management.*—He would not be obliged to assume responsibility for detailed administration except in the case and in the manner indicated below. It would be his duty to see at all times that the administration was reasonably efficient and the accounting system honest and accurate. But since the interests of

the Allies are not affected so long as the revenues are sufficient, with an adequate margin, to meet the annual charges, it would not be his duty in such circumstances to interfere with the details of control.

He would therefore not normally be obliged to insist on the exact tariffs or the exact form of administration which would, in his view, secure the utmost yield, and he would not therefore be obliged (unless the need arose) to assume the responsibility of detailed direction with the administrative expense on staff, etc., which that would involve nor would he be required to have such an elaborate and expensive accounting and calculating personnel as would enable him to certify that every mark was accurately accounted for (which is obviously a very different thing from seeing that the system is honest and efficient).

If the need arose his control would become automatically more active, more responsible, more difficult and, of necessity, more expensive. For if the revenues were in danger of being insufficient, it would be his duty to take every possible measure to increase their productivity. This increase in the active character of the control would be in exact proportion to the need for it. He would thus reform and direct administration in detail only if and so far as necessary.

D. *The technical control* would consist, in the ordinary course, of the right:

(a) to obtain all information and examine all books;

(b) to visit and inspect the factories subject to duties, and to ascertain that approved standards are maintained;

(c) to send experts to report and advise and, in case of actual necessity arising, to exercise detailed control;

(d) to propose higher technical standards;

(e) to require prior advice of all administrative regulations.

In settling the constitution of the control body, it should be borne in mind that it may be concerned with the issue of bonds guaranteed by the said assigned revenues, if it is desired to create an international bond other than the railway one.

The German Government should be asked not to reduce the rate of the assigned revenues without the consent of the commissioner, which would not be given until the consultative committee had had an opportunity of considering the proposal and approved it by a majority; on the other hand, it is considered necessary that the German Government should be encouraged, regard being had to the rates prevailing in other countries, to effect increases in the taxation of alcohol, beer and sugar.

The above system makes it unnecessary in relation to the problem of security, to insist on an increase in any particular tax, though we suggest to the German Government that it is to their interest, especially having regard to the rates prevailing in other countries to effect increases in the taxation of alcohol, beer and sugar. But all interference in the German Government's tariff policy is to be avoided.

To sum up this subject we would lay down the following general principles:

1. The main lines on which the control should work ought to be decided by the countries interested. These main lines establishing the principle of a control developing automatically as required, and becoming complete control as soon as the revenues appeared to be insufficient, should therefore be laid down in protocols signed by all the countries whose interests are mainly involved.

2. These main lines should be elaborated into detailed instructions by international experts (in practice of the nationalities of the countries interested).

3. With this safeguard, the execution of the control is entrusted to a single impartial person (with the necessary staff) so as to secure the rapid and consistent administrative decisions required for an efficient control.

4. His responsibility to the Reparation Commission should not be of a day to day order, but a periodical report should be made by him upon the condition and yield of the gage revenues.

5. In the event of the revenues for a given year proving insufficient, the whole system outlined in this scheme (working of the railways, a mortgage on industrial property, the control of the revenues assigned as security) will be prolonged as required for the purpose of making good the deficit.

The committee desires to express its high appreciation of the valuable and efficient cooperation received throughout its task from the general secretary, Mr. Andrew McFadyean, and to thank his assistant, Monsieur Denis, the interpreters, and all the staff for their ungrudging services.

CHARLES G. DAWES, *Chairman.*
OWEN D. YOUNG.
ROBERT M. KINDERSLEY.
J. C. STAMP.
J. PARMENTIER.
EDGARD ALLIX.
ALBERTO PIRELLI.
FEDERICO FLORA.
E. FRANCQUI.
MAURICE HOUTART.

Paris, April 9, 1924.

ANNEX NO. 1 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

PLAN FOR THE ORGANIZATION OF A BANK OF ISSUE IN GERMANY

I. Name and Location

The Bank, hereinafter designated as the "New Bank," shall bear a new and suitable title, unless, in conformity with paragraph *(b)* Section III below, the Organization Committee shall decide to use the Reichsbank for putting the present plan into operation. It shall be a private corporation, and its charter shall be for fifty (50) years. The new Bank shall have its principal office in Berlin and such branches and agencies as its Managing Board shall determine.

II. Capital

a. The Bank shall have a cash paid-up capital of four hundred million (400,000,000) gold marks, which shall be in registered or bearer shares of one hundred (100) marks each. These shares shall be issued as follows:

1,000,000 shares to represent assets of the Reichsbank;

3,000,000 shares for subscription in Germany and abroad.

b. All shares shall be alike, and after the initial subscriptions have been accepted, no restrictions shall be imposed upon their purchase and sale, other than such general restrictions of German law as shall apply to the purchase and sale of shares of other banks.

c. Shares whether sold in Germany or abroad shall be paid for entirely in gold, and/or foreign bills, at their current gold values.

d. Subject to the preceding provision of this Section, the shares of the new Bank shall be allotted and sold on such terms as to prices, times of payment and other conditions, as are most advantageous to the Bank.

III. Organization Committee

a. For the purpose of taking the preliminary steps for the Bank's corporate organization, there shall be created a temporary committee, to be known as "The Organization Committee." This Committee shall consist of two (2) members, the President of the Reichsbank, and one (1) person who shall have been a member of one of the Committees of Experts acquainted with the discussions which resulted in the drafting of the plan for the Bank.

b. The Organization Committee shall have power generally to interpret any ambiguities appearing in the plan, provided always such interpretation shall not interfere with the principles involved. It shall also have power if it deems wise, to carry out this plan by the transformation of the Reichsbank, under suitable legislation, rather than by the organization of a new corporation. It shall frame the statutes regulating the administration of the Bank. These statutes shall in particular include provisions concerning:

1. the form and character of the share certificates of the Bank;

2. the formalities to be fulfilled for the transfer and pledging of the registered share certificates;

3. the cancellation of share certificates lost or destroyed;

4. the method by which the German shareholders shall elect the German members of the General Board;

5. the nature of the reports published by the Bank, as well as the method and place of their publication;

6. the nature and duties of the permanent Committees, of the Managing Board and the officials of the Bank;

7. the administrative Departments to be created within the Bank;

8. the date and place of the regular meetings of the Managing Board and of the General Board;

9. the special meetings of the Managing Board and of the General Board.

IV. Administration and Management

The Bank shall be administered by a Managing Board, under the chairmanship of a President, all of whom shall be of German nationality.

V. The President of the Bank

a. For the purpose of this memorandum only, the Chairman of the Managing Board and of the General Board is hereinafter called "The President"; he shall be the managing director of the Bank. Subject to the limitations imposed by law, he shall perform such duties as are assigned to him by the Bank's statutes.

b. The President may be elected from among the members of the General Board, or chosen from outside the Board. The election by the Board of a non-member as President shall operate to vacate automatically the seat of that German member of the General Board having a term of two (2) years or more yet to run, whose election was obtained by the smallest share vote, unless some other member of the General Board, having a two (2) years' term or more yet to run, shall resign at the time, and his resignation be accepted by the Board. A President, elected from outside the General Board shall, by the fact of his election, become a member of the Board.

c. The first President shall be the President of the Reichsbank; his term of office shall be six months. Subsequently, the President, who must be of German nationality, shall be appointed by a majority vote of not less than nine (9) members of the General Board, of which

majority at least six (6) votes shall be the votes of German members; this appointment shall be countersigned by the President of the Reich.

d. The President shall direct the Managing Board and shall take the chair at its meetings. In case of a tie vote, he shall have the casting vote. He shall appoint the officials of the Bank on the recommendation of the Managing Board. He shall organize the distribution of their work and duties in the Bank, and shall exercise disciplinary powers over the officials and employees, these powers being provided for in a special clause of the statutes to be approved by the General Board.

VI. Managing Board

a. The administration of the Bank shall be entrusted to a Managing Board which shall be the administrative and executive body. This Board shall be under the chairmanship of the President. It shall adopt its decisions by majority vote and in conformity with the regulations laid down in the statutes and by law. In particular it shall direct the currency, discount, and credit policy of the Bank. It shall fix the rates of interest and shall draft all regulations concerning the policy of the Bank.

b. The members of the Managing Board shall be appointed by the President for a period to be fixed by the Organization Committee, subject to the approval of the General Board, whose decision in this connection shall be adopted by a majority of nine (9) votes, at least six (6) of which shall be given by the German members; these appointments shall be countersigned by the President of the Reich.

c. The members of the Managing Board shall occupy no other remunerated post, neither shall they accept any honorary post without the previous consent of the General Board.

d. The salaries and pensions of the members of the

Managing Board and of the President shall be fixed by the General Board, the salaries and pensions of the senior staff of the Bank shall be fixed by the Managing Board with the approval of the President, and in case of the junior staff, by the Managing Board alone.

e. The Managing Board may, if they think fit, obtain the assistance of a consultative body composed of German members chosen from agriculture, commerce and industry.

VII. General Board

a. There shall be created a General Board, consisting of fourteen (14) members hereinafter called "the Members of the General Board." One-half (½) of these members shall be of foreign and the other half (½) of German nationality.

b. Each member of the General Board shall be chosen for a period of three (3) years, except in the case of the first election or appointment. In the case of the first term of office, three (3) German members and three (3) foreign members shall serve for a term of one (1) year; two (2) German members and two (2) foreign members shall serve for a term of two (2) years, and two (2) German members and two (2) foreign members shall serve for a term of three (3) years. At the first meeting of the General Board chosen, the members shall decide, by lot, the term for which each shall serve, namely, one, two, or three years.

c. Subject to the provisions of paragraph *(b)* of this section, and to the provisions of this plan that apply to all members of the General Board, members of German nationality shall be chosen in such a manner and under such conditions as the stockholders of German nationality shall decide, in accordance with German law. The manner and conditions so decided upon shall be incorporated in the statutes. The manner of selecting the first group of German members shall be determined by the Organization Committee as provided for in Section III of this plan. No

plan shall be adopted for the first selection of German members that does not meet with the approval of the President of the Reichsbank.

d. The foreign members of the first General Board shall be appointed by the Organization Committee. They shall be chosen with due regard to their professional qualifications and financial experience. In making the appointments, the Organization Committee may consult the principal foreign banks of issue and/or any other authorities in financial matters whose advice it may desire.

e. In case of vacancy in a position of a foreign member of the General Board, arising from death, resignation or other cause, there shall be a new election of another person of the same nationality to fill the vacant place. This election shall be by the foreign members of the Board who are in active membership at the time this election is held. Unanimity less one vote shall be necessary for an election. The new member shall always be chosen from among the nationals of the country of the member whose vacancy he is to fill. Before electing any foreign members of the Board the Board shall consult, with reference to said election, the Central Bank of Issue of the country whose national is to be chosen and/or any other financial authorities of that country whom it may desire to consult.

f. The foreign members shall be chosen, one from each of the following nationalities, British, French, Italian, Belgian, American, Dutch, and Swiss.

g. On the unanimous vote of the General Board, the number of German members may be increased.

h. No Government official, or other person receiving compensation from the German Government, or from any foreign Government shall become one of the General Board.

i. Except as otherwise provided for by the Bank's statutes, decisions of the Board shall be by a majority vote of the ten (10) members, or by a simple majority vote if the President and the Commissioner are included in the

majority. Should a member not be able to attend a meeting of the Board, it will always be open to him to empower one of his colleagues, by registered letter or by telegram, to vote for him and on his behalf.

j. At each of its meetings, and at least once every month, the General Board shall examine the reports submitted to it by the President and the Commissioner. It shall adopt decisions on all the proposals made to it by the President and the Commissioner, provided that these decisions do not encroach upon the rights reserved to the President and the Managing Board as specified in Sections V and VI above.

k. The metal reserve of the Bank and the office for the printing of the notes shall be in Germany, but the General Board may, by a three-quarters (¾) majority vote, decide that either or both be transferred abroad to a neutral country.

VIII. The Commissioner

a. The Commissioner, who shall be a foreigner, shall be elected by a majority vote of not less than nine (9) members of the General Board, of which majority at least six (6) votes shall be those of foreign members. The Commissioner's term of office shall be fixed by the Organization Committee.

b. The Commissioner may be elected from among the members of the Board of foreign nationality, or may be chosen from outside the Board, from citizens of any one of the foreign countries represented on the Board. The election by the Board of a non-member to the position of Commissioner shall operate to vacate automatically, the position of the citizen of the country of which the Commissioner is a citizen. A Commissioner elected from outside the Board shall, by the fact of his election, become a member of the Board.

c. If, at the first election, the person chosen as Com-

missioner should be a member whose term, as decided by lot, in accordance with paragraph *b* of Section VII of this scheme, should only be one year, the term of this member shall automatically be increased to two (2) years. In this case, one of the two foreign members who have been assigned to two (2) years' term, shall have his term reduced to one (1) year. The decision as to which of the two foreign members shall have his term thus reduced from two (2) years to one (1) shall be made by lot.

d. It shall be an essential duty of the Commissioner to enforce the provisions of the law and the statutory regulations relative to the issue of notes and the maintenance of the Bank's reserves which guarantee that issue. To this effect, the Commissioner shall have the right to have furnished to him all statistics and documents which he may deem useful for the accomplishment of his task, and whenever it appears to him necessary, he may make any investigations either in person or through his assistants. He shall be entitled to be present at the meetings of the Managing Board in Berlin.

e. The office entrusted with the custody of the reserve of notes shall only deliver notes when authorized by the Commissioner so to do.

f. The Commissioner shall be bound to the greatest secrecy in regard to all information he may obtain on the commercial operations of the Bank.

IX. Loans, Discounts and Investments

a. The Bank shall make no loans or discounts having a maturity at the time the advance is made, in excess of three (3) months.

b. The Bank shall discount no notes or bills bearing less than three (3) names of known solvency, except that for one name there may be substituted collateral in the form of warrants relating to bona-fide commercial transactions or to goods. Such definition shall not be taken as

including any notes issued or bills drawn in financial transactions or secured by stocks, bonds or other investment securities but may include Treasury Bills of the German Government.

c. The Bank may, with the special authorization of the General Board voting in the conditions laid down in paragraph *(i)* of Section VII, accept the long term bonds of the Reich as collateral for loans with maturities not exceeding three (3) months, if the loans bear two (2) responsible names, in addition to the collateral, one of these names being the name of a commercial bank doing business in Germany. Provided: that loans collaterally secured by the long term securities of the Reich shall never exceed the amount of the Bank's net paid-in capital and surplus, except by the unanimous vote of all the members of the General Board save one.

d. The Bank shall make no loans nor advances on the security of real estate, mining property, oil property or stock shares; nor on the security of Government obligations, except as otherwise provided for in this plan. The Bank may, however, take mortgages or titles to such property, stock shares and Government debt bonds as additional security for loans previously made in good faith in accordance with provisions herein made.

e. Subject to the provisions contained in Article *a,* the Bank shall make no loans, discounts, or other advances directly or indirectly, to the German Reich, any German State, Communes or other German Governmental units, or to any foreign Government or Governmental units, nor shall it invest its funds in the bonds, debentures or other debt of any such Government unit, except as otherwise specifically authorized by its constitutive law. The deposit accounts and current accounts in the Bank, of the German Reich, the German States, the German Communes or other German Governmental units, shall never show a debit balance.

f. The Bank shall not accept time bills of exchange drawn against it.

g. The Bank may not buy or sell merchandise, produce, real estate or stock shares of other corporations for its own account.

h. The restrictions contained in the preceding paragraph shall not operate to prevent the Bank from buying such real estate, equipment and supplies as it needs for its own banking business, or from selling such property as may come into its possession in connection with the guarantee of statutory loans. Moreover, the Bank shall not be prevented, by the above restrictions, from buying in property where it needs to do so, in order to protect itself in the collection of statutory loans previously made in good faith and not paid at maturity.

X. Service of the Reich's Treasury

a. The Managing Board is authorized to make advances from time to time to the Reich, but the amount outstanding at any one time shall never exceed 100 million marks. Such advances shall, in no case, be for a longer period than three months and in no case shall the Reich be indebted to the Bank at the end of the Bank's financial year, which shall coincide with that of the Reich. In consideration of these facilities, the Reich and its Treasury shall conduct all their domestic and foreign banking business through the medium of the Bank.

b. The Managing Board shall also be empowered to grant advances to the Post Office and the Railways for reasonable amounts on condition that these organizations shall entrust the Bank, except in so far as the Bank might modify this condition, with the whole of their Treasury Service; but the total amount of loans outstanding to the Post Office and the Railways together shall never exceed 200 million gold marks.

XI. Service of the Reparation Treasury

The Bank will receive on deposit, sums paid for reparations, it being understood that the relationship between it and the Committee entrusted with Reparation receipts shall be solely those of banker and customer.

This Treasury Service will proceed in conformity with the provisions of Annex. . . to the General Report. The maximum amount to be held on deposit for reparation account shall at no time exceed two (2) milliards of marks in conformity with Section X (*a*) of this Annex, except as otherwise provided therein.

XII. Bank Notes

a. The Bank shall have the exclusive right of issuing and circulating bank-notes in Germany during the period of its charter.

b. The German Government may not itself issue any kind of paper money for circulation in Germany, during the period of the Bank's charter, nor shall it permit any German State, Commune, City, other governmental unit, corporation or private individual, to issue or circulate paper money in Germany during the period of the Bank's charter, with the exception of the Banks of Baden, Bavaria, Saxony and Wurtemberg, which shall retain their charter of issue for sums not to exceed their present legal quota. The notes of the Rentenbank shall be gradually withdrawn from circulation under the conditions prescribed in Section XV and the Appendix hereto.

c. During the period of the Bank's charter, the Reich shall not issue any coins for circulation in Germany (except gold coins, containing approximately their full value in gold metal) of a larger denomination than five (5) marks; and shall not issue coins of five (5) marks or less, in excess of twenty (20) marks per capita of her popula-

tion. All coins, other than gold coins, issued by the Government, shall be issued through the Bank. They shall be received by the Government in unlimited quantity at their nominal value, in payment of all taxes and other government dues.

d. The bank may issue notes for circulation, against gold coin or bullion, statutory discounts as defined in Section IX, demand credits in foreign banks and foreign commercial trade bills, with maturities of three (3) months or less, taken at their present gold values at current rate of exchange.

e. The notes of the Bank, as well as metallic currency, shall be receivable in unlimited quantities for all taxes and other government dues in Germany. The notes shall be unlimited legal tender, unless otherwise specifically provided by contract, for all debts, public and private.

f. The notes of the Bank shall be accepted at their nominal value for all payments made to the Bank, both at the head office of the Bank in Berlin, and at all branches of the Bank located in Germany.

g. Notes shall be payable to bearer at the head office of the Bank in Berlin on presentation. The notes shall also be payable on presentation at the other offices and branches of the Bank, to the extent permitted by their cash reserves and monetary requirements. Payments may be made in any of the following forms, at the option of the Bank:

1. German gold coins of the present legal standard of weight and fineness, at par;
2. gold bars, in denominations of not less than one (1) thousand gold marks, and not more than thirty-five (35) thousand gold marks, at their pure gold equivalent in German gold coin of the present legal standard of weight and fineness;
3. demand drafts, payable in gold or in foreign cur-

rencies at current market gold values, and drawn on funds located abroad in solvent banks to be specified by the Bank's statutes provided that the premia above the gold pars (or gold values, in the case of currencies not on a gold basis) charged by the Bank for such drafts shall never exceed the amount necessary to cover shipping expenses, including interest for the time of transit, on gold bars shipped in substantial quantities from Berlin to the foreign financial centre on which the draft is drawn.

The Committee is of opinion, however, that, at the inception of the Bank, conditions will be unfavorable for the application of the above rule of convertibility in this event, this rule may therefore be temporarily modified by the affirmative vote of every member but one of each of the following groups:

1. The Organization Committee.
2. The Managing Board.
3. The General Board.

In case of such modification, the Bank shall make all possible efforts and use all the means at its disposal in order to maintain the rate of exchange of the mark at as near gold parity as possible. Furthermore, in case of modification of the above mentioned rule of convertibility of notes, a return to convertibility will be permanently established as soon as possible, by a simple majority vote of the General Board, and of the Managing Board.

h. While the Bank shall not make reimbursement for notes that have been lost or completely destroyed, it shall replace worn or torn notes, on application, by notes in good condition, at their nominal value; provided that such replacement shall not be required in the case of any note unless the part of the note presented shall constitute more than one-half of the note.

i. The notes of the Bank shall bear the facsimile signature of the President and the seal of the Commissioner.

XIII. Reserves

a. The Bank shall always carry a normal reserve of at least thirty-three and one-third (33 1-3)% of the total amount of its notes outstanding, subject to the following qualification:

In exceptional circumstances, the reserve against notes may be reserved below thirty-three and one-third (33 1-3)% on the proposal of the Managing Board, by a decision of the General Board; but said decision of the General Board shall require the affirmative vote of every member of the Board save one. In case of such a reduction in the reserve, the Bank shall incur the following penalties, the proceeds of which it shall pay to the Reich; whenever the reserve against notes shall be less than thirty-three and one-third (33 1-3)% of the notes outstanding and shall so continue for more than one week the Bank shall pay the following deficiency tax upon the amount by which the said reserve is less than thirty-three and one-third (33 1-3)% of the notes outstanding:

When the reserve is below thirty-three and one-third (33 1-3)% and not below thirty (30)% a tax of three (3)% per annum;

When the reserve is below thirty (30)% and not below twenty-seven (27)%, a tax of five (5)% per annum;

When the reserve is below twenty-seven (27)% and not below twenty-five (25)%, a tax of eight (8)% per annum;

When the reserve is below twenty-five (25)% a tax of eight (8)% per annum plus one (1)% per annum for each one (1)% the per cent tax figure is below twenty-five (25)%.

b. No discount rate or rediscount rate shall be below five (5)% per annum when the reserve mentioned in the preceding paragraph shall have continuously, for one week or more, been below thirty-three and one-third (33 1-3)% of the bank note liabilities there mentioned.

c. Whenever a deficiency tax is payable, a percentage equal to at least one-third (1-3) of the percentage rate of the tax payable shall be added to the Bank's discount rate and rediscount rate, in addition to any increase in the said rates required to comply with the provisions of the preceding paragraph.

d. The above-mentioned legal reserve may be kept in gold bars or gold coin, at any office of the Bank, and/or in the form of demand deposits, made payable in gold or its equivalent, at the rates at which the deposits were made, in banks of high standing located in foreign financial centres.

e. The Bank shall also hold a special reserve of gold and gold deposits, of the same character required to be held against its notes in circulation, to the amount of twelve (12)% of its deposit liabilities. Whenever the above reserve is continuously, for one week or more, below said twelve (12)%, the Bank shall pay a deficiency tax of four (4)% per annum on the amount by which the reserve is less than twelve (12)% and not less than ten (10)%; a tax of eight (8)% per annum on the amount by which it is less than ten (10)% and not less than eight (8)%; and a tax of ten (10)% per annum in addition to said eight (8)% for each one (1)% by which the percentage figure is below eight (8)%.

f. In order to assure adequate liquidity in the assets securing the Bank's deposit liabilities, the Bank shall at all times hold in addition to its afore-mentioned gold reserve of twelve (12)% demand deposits in Germany and abroad, cheques on other banks, and statutory notes and bills of a

commercial character, payable at call or on time with maturities of less than thirty (30) days to the amount of not less than thirty (30)% of the Bank's total deposit liabilities.

g. The above-mentioned reserves and the liquid assets above described shall be segregated for the service of the Bank's deposits.

XIV. Profits

The net profits of the Bank, at the end of each financial period, shall be employed as follows:

a. Twenty (20)% shall be transferred to surplus or reserve until the Bank's actual net paid-up capital and surplus shall amount to twelve (12)% of its average liabilities on circulating notes, on the fifteenth day of the six preceding months. If the ratio shall again fall below this twelve (12)%, the above-mentioned allotment of twenty (20)% of the net profits to surplus or reserve shall continue. When and so long as the ratio of the Bank's net capital and surplus or reserve to its average liabilities on circulating notes, as above computed, shall exceed twelve (12)%, the Bank may use its discretion as to the percentage of its net profits it will transfer to surplus or reserve provided that the percentage thus transferred shall never exceed twenty (20)%.

b. A sum shall be assigned to the payment of dividends sufficient to pay eight (8)% per annum on the Bank's shares.

c. The balance of the net profits shall be divided as follows:

1. One-half (½) to the shareholders, in dividends or to a special fund to be used for the maintenance of a uniform dividend policy.
2. One-half (½) to the Government, as a franchise tax

for the Bank's exclusive privilege of issuing circulating bank-notes.

d. The dividends of the Bank and other income derived from its capital shares owned by foreigners residing abroad, shall be exempt from all German income taxes, present and future; provided that this exemption shall not apply to general taxes imposed in Germany upon the real property of the Banks in general. The Bank, however, in consideration of the percentage of profits accruing to the Government under paragraph *c* 2, shall not be subject to any corporation tax or business tax levied in Germany by the Reich, the States or any other governmental unit.

e. Such privileges not inconsistent with this plan, now enjoyed by the Reichsbank, as may be specified by the Organization Committee as desirable and advantageous to the new Bank shall be given to it.

XV. Liquidation of the Rentenbank

The Rentenmarks shall gradually be withdrawn from circulation by the Bank in accordance with the provisions contained in the Appendix attached.

XVI. Dollar-schatzanweisungen

(treasury bills in dollars)

a. The German Government shall abandon all its rights to the proceeds from the liquidation of the Reichsbank (unless the present plan is put into execution by means of the transformation of the Reichsbank), in return for which the latter will give the Government an undertaking to assume responsibility for the repayment of the said bills not in excess of 210 million gold marks, under conditions to be settled by the Reichsbank with the holders of these bills.

b. At the same time, in order to guarantee the good faith of this operation, that is to say, in order to guarantee the Reichsbank against any loss resulting from this operation, the German Government shall hand over to the Reichsbank gold bills for an amount equal to and falling due at the same date as the dollar bills in circulation. As soon as the liquidation of these dollar bills has been completed, the Reichsbank will return to the German Government the portion (if any) of the bills which it has received, and which has not been employed in ensuring the liquidation.

XVII. The Reichsbank

a. If the present plan is put into execution by means of the transformation of the Reichsbank, the latter shall redeem the outstanding circulating notes in its new notes, at the rate of one billion (1,000,000,000,000) marks to one (1) gold mark. The old notes shall be immediately withdrawn from circulation and cancelled.

b. The Reichsbank, in case it is continued, shall meet the same reserve requirements against the outstanding notes which it undertakes to exchange, in accordance with the provisions of paragraph *a* of this section, as are required to be held against bank notes outstanding by Section XIII of this plan.

c. If the Reichsbank is to be liquidated, this operation will be carried out by the new Bank which would be then set up, and which would have to assume responsibility for, or itself carry out, the exchanges provided for in paragraphs *a* and *b* above.

XVIII. Penalties

A penalty in the form of fine or imprisonment or both shall be provided for the punishment of any person or persons wilfully giving incorrect information, directly or

indirectly, to the President, the General Board, the Commissioner or his assistants.

XIX. Measures to be Taken by the German Government For the Execution of the Plan

All the undertakings which the German Government will have to enter into in connection with the Bank, for the execution of this plan, including the assignment for the withdrawal of the rentenmark, of funds, to be received from the rentenbank's mortgages, shall be embodied in a special contract between the Bank and the German Government. This contract as well as the Statutes of the Bank, shall be duly approved by the German Parliament.

APPENDIX TO ANNEX I

THE LIQUIDATION OF THE RENTENBANK

(Appendix provided for in Section XV of the plan for the bank.)

The Deutsche rentenbank was founded, and its operations regulated, by the decree of October 15, 1923.

The capital and the initial reserve were fixed by this decree at 3,200,000,000 rentenmarks, to be furnished half by agriculture and half by industry and commerce, including the banks.

The rentenbank holds a general mortgage, expressed in gold marks, on industrial, agricultural, and commercial property, amounting to 4 per cent of the value of this property as assessed for the Wehrbeitraggesetz.*

These mortgages bear 6 per cent interest for the benefit of the rentenbank.

The rentenbank is authorized to issue bank notes expressed in rentenmarks up to the amount of the capital and initial reserve (3,200,000,000 gold marks).

* The amount of this mortgage already amounts to 3,700,000,000 gold marks.

The rentenbank must open credits to the Reich during the two years following its foundation up to the amount of 1,200,000,000 rentenmarks, of which 900,000,000 will bear 6 per cent interest and 300,000,000 will bear no interest. The rentenbank is authorized moreover to open credits to the Reichsbank and to the private banks up to 1,200,000,000 rentenmarks, in order to finance private economy.

Up to the present the rentenbank has placed in circulation:

1. Seven hundred million, which have been delivered to the Reichsbank in order to provide for the credits to be granted by the latter to German manufacturers and merchants. This sum is therefore guaranteed by drafts or credits redeemable in rentenmarks. If and when the rentenbank is liquidated, no attention need be paid to them.

2. One milliard one hundred million rentenmarks which have been advanced to the Reich without any security but the signature of the latter, 900,000,000 of which bear 6 per cent interest per annum and 200,000,000 bear no interest.

In so far as concerns this latter sum of 1,100,000,000 the new bank (or the Reichsbank, if it is maintained) would assume the obligation vis-a-vis the holders of these notes to redeem them gradually within 10 years. To this effect the rentenbank would undertake to remit to the bank, as fast as they came in, all sums received from its debtors, whether from the property holders affected by the rentenbank mortgage or from the State, up to the sum of 1,100,000,000.

This undertaking of the rentenbank vis-a-vis the bank would be covered by all the mortgages and guarantees which it holds, as well as by the guarantee of the German Government itself.

It should, moreover, be understood that all profits accruing to the Reich in virtue of its participation in the bank would be assigned by priority to the amortization of its debt of 1,100,000,000.

As soon as the payments by the rentenbank or by the Reich itself, as stated above, reach the figure of 1,100,000,000 the German Government and the rentenbank will be released from all liability vis-a-vis the bank.

ANNEX NO. 2 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

BASIS OF COMPARISON

1. In addition to the standard contribution referred to in paragraph VIII *c*, there shall be paid for 1929-30 and following years a supplementary sum according to the growth in prosperity of Germany. This increase in prosperity for any year shall be measured by the extent to which the index, as defined below, on the statistics of the completed preceding year, exceeds the average statistics of the base years.

COMPONENTS OF THE INDEX

2. For the purpose of computing the index, the following statistics shall be employed:

a. the total of German exports and imports taken together;

b. the total of budget receipts and expenditure taken together, including those of the States of Prussia, Saxony and Bavaria (after deducting from both sides the amount of the Peace Treaty payments included in the year);

c. railroad traffic as measured by the statistics of the weight carried;

d. the total money value of the consumption of sugar, tobacco, beer and alcohol, within Germany (measured by the prices actually paid by the consumer);

e. total population of Germany (computed from the last available census data, vital statistics and emigration records);

f. the consumption of coal (and lignite reduced to coal equivalent) per capita.

THE INDEX BASE

3. In computing the *base*, the average statistics for the *three* years 1927, 1928 and 1929 shall be taken for *b* budget receipts and expenditure, for *e* population and for *f* coal consumption per capita, and for the *six* years 1912 and 1913, 1926, 1927, 1928 and 1929 for the other categories (after appropriate adjustments for the differences in population and the altered gold values to make the three earlier years comparable with the three later years in this respect). The percentage change for each of these six groups, compared with the base, shall be separately computed and an arithmetical average of the six percentage results taken as the index.

PAYMENT TO WHICH THE INDEX IS APPLIED

4. The index percentage shall be applied to the amount of the standard payment, viz. 2,500 millions, to give the supplement for the year, except that for the five years 1929-30 to 1933-34 it shall apply to 1,250 millions, or one half of the standard payment only.

MINUTE ADJUSTMENTS IGNORED

5. The supplementary payment is to be reckoned only for each completed half per cent of the index, *i. e.* an index average of 11.35 per cent. would be reckoned as 11 per cent.

COMPUTATION OF SUPPLEMENT

6. For the year 1929-30, the computation of the supplement shall be made after the end of that year by comparing the statistics of 1929 itself with the index base.

DEFICIENCIES

7. In the event of the index in any year producing, as the supplement, a minus quantity, the basis payment should continue to be made, but subsequent supplementary payments shall not accrue due until allowance has been made therefrom for such deficiency or "minus" payment of previous years.

DIFFICULTIES IN APPLICATION

8. Any disputed points upon the application of the statistics of this index shall be referred to the Finance Section of the League of Nations for arbitration.

CHANGES IN THE VALUE OF GOLD

9. The German Government and the Reparation Commission should each have the right in any future year, in case of a claim that the general purchasing power of gold as compared with 1928 has altered by not less than 10 per cent, to ask for a revision on the sole and single ground of such altered gold value. The alteration to be made may apply both to the standard contribution and the supplementary payment. Failing mutual agreement, a decision should be given by an arbitral committee appointed by the League of Nations. After decision, the altered basis should stand for each succeeding year until a claim be made by either party that there has again been a change, since the year to which the alteration applied, of not less than 10 per cent.

The alterations under this paragraph should be made by reference to such generally approved index numbers of prices (German or non-German), singly or in combination as the arbitration may decide.

ANNEX NO. 3 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

NOTE BY THE FIRST COMMITTEE OF EXPERTS

Of the assets and revenues of the German Reich and its constituent States subject to the application of Article 248 of the Peace Treaty, the German railway system is undeniably the most important and also that which can be the most easily utilized for the purpose of reparation.

The German railway system comprises about 53,000 kilometres of lines, and the rolling-stock will very shortly amount to:

Locomotive engines (excluding electric and motor engines)	30,850
Passenger vehicles	69,253
Wagons	748,753

A considerable portion of this rolling-stock is of recent construction. Two-thirds of the whole (18,000 locomotives and 500,000 passenger vehicles and wagons) were brought into service in the last ten years. The rolling-stock at present possessed by the German railway system is very superior both in quality and quantity to that which was in use before the war.

Speaking generally, it may be said that the equipment of the German railways is modern and fully up to the level of the latest improvements in railway technique.

The capital cost of the system amounts to not less than 26 milliard gold marks.

The Experts called in the services of eminent railway specialists, and requested them to make a study of the German railways; their report is attached.

GENERAL REPORT ON THE GERMAN RAILWAYS MADE TO THE FIRST EXPERT COMMITTEE

BY SIR WILLIAM ACWORTH AND M. LEVERVE

26th March 1924.

In our earlier Reports we described the situation of the German railways and replied to various questions asked by the Committee, especially as to the amount of net revenue which we considered they could yield for reparation purposes. We have now, as requested by the Committee, brought together in a single document the essential portions of these reports together with our own conclusions.

We desire to thank the German Minister of Railways and his staff for the manner in which they have assisted our enquiry in Berlin with information both verbal and documentary. In the short time at our disposal it has naturally not been possible for us to push our investigations very far, but we trust that the Report which we now present is adequate for the purposes of the Committee, and we think its substantial accuracy may be relied on.

CAPITAL INVESTED IN THE GERMAN RAILWAYS

In a preliminary report we stated that the capital value of the German railways might safely be taken at not less than 20 milliard gold marks. An official publication shows that the debt of the several States specifically entered as railway debt, less that portion of it applicable to the ceded territories, amounted in 1914 to 17.93 milliard gold marks. In March, 1920, at which date the railways were transferred from the ownership of the several States to that of the German Reich, the invested capital was reckoned as

25-28 milliard gold marks. This large increase is explained by the fact that at the date of the transfer:

a. the value of the railways of the separate States was written up to conform to the real amount of capital that had been invested in them, much of which had never been or had ceased to be represented by railway debt:

b. there was added to the old capital the value of the additions made during the war. Between March, 1920, and March, 1923, the capital invested was further increased to 25.86 milliard g. m. The expenditure for the current year and that which will still need to be incurred in payment for commitments already entered into will put the final figure well over 26 milliard g. m.

The above figures represent capital invested, which is sometimes a very different thing from capital value. But in this case the capital value of the German railway system which comprises 53,000 kilometres at 500,000 gold marks per kilometre may be taken to be fully equal to the capital invested. Now a large part of the system is double tracked; the lines, stations, yards and buildings have been constructed to a high standard, and they are very amply equipped with up-to-date rolling stock. A comparison with the capital cost per kilometre of the railways of other important countries, taking account of all the factors on both sides, gives good grounds for saying that the German figure of investment is by no means an excessive representation of actual cost.

NET REVENUE ATTAINABLE

We think that a net annual revenue of one milliard g. m. per annum can reasonably be expected from the German railways. This is very slightly more than the net revenue earned before the war; but it was then earned very easily. No attempt was made to maximize net

revenue, which was much more than sufficient to meet the interest on the railway debt.

On the one hand, the tariffs were kept low; especially for passengers. The guiding principle was, as has been recently expressed in a brochure published by Dr. Sarter, whose statement, as he is a highly placed official in the Transport Ministry, may be taken as authoritative. "The State Railways ought primarily to have regard to the progressive development of the economic life of the country and to treat the attainment of net revenue as only of secondary importance."

On the other hand, the operating expenses were unduly high; the staff was unnecessarily large; and magnificent stations and enormous shunting yards were worked at great expense. Moreover, as is shown by the figures which we have given above, the working expenses included year by year large sums for improvements and additions which might properly have been charged to capital.

It may be thought—seeing that for some years past the gross receipts of the German railways have not covered their expenses, and that recently the expenditure was several times as great as the receipts, while even now the earnings are only equal to the expenditure—that this estimate of ours is unduly sanguine.

But it is to be remembered that since the war almost every country has gone through a similar experience. Even in the United States, where there was no currency depreciation, the net income of the railways in 1920 was almost negligible; whereas in England, where currency depreciation is quite small, the receipts in 1921 fell short of the expenses. But in both countries the situation has now completely changed, and if in other countries the railways have still not regained financial equilibrium, experience sufficiently shows that this phase is only temporary. And Germany has one special circumstance of the first im-

portance in her favour. On the railways of England and America, the wages of the railway staff are roughly double what they were before the war. No such advance has taken place in Germany. On the contrary, the average wage is at present, we are informed, only 75% of the pre-war wage. It is proposed in the current year to increase this percentage to 93% of the pre-war average. But there is no prospect of any such increase above the pre-war standard as has taken place in the two countries mentioned. And this for two reasons: the cost of living has not increased in Germany, as it has here, and, as German wages in other occupations have not risen, railway wages do not compare unfavorably.

Naturally we do not suggest that a milliard of net revenue is attainable at the outset. But we think a substantial sum can be obtained very shortly, and that the full amount should be reached within a period of three years. It should be arrived at in the manner following:

During the war there was imposed in Germany, as in other countries, a transport tax. This tax still continues to be levied. It is included in the rates charged to the public but is paid over by the railways direct to the Finance Ministry and forms therefore no portion of the railway revenue. It is a tax on the gross receipts, and is fixed at 7% on all receipts from freight traffic other than coal, and at 10% to 16%, according to class, on passenger traffic. On the average it amounts to 6% of the total gross receipts. It is estimated to produce in the year 1924, 227 million gold marks. If in future years the traffic increases, or if the same volume of traffic is charged at a higher rate, naturally the proceeds of the tax will increase proportionately. It seems safe to assume that its yield will not fall below the present figure. Moreover, as it is levied on the gross and not on the net income, it is independent of any variations in the cost of operation. If, as

we recommend, the German railways in future are required to pay over the proceeds of this tax to the Reparation Commission, the Commission will have from the outset a safe and important source of revenue at their disposal.

There remains a sum of 800 million gold marks in round figures to be obtained, and it can, in our judgment, be obtained as net profit on the railways, on condition that the tariffs are fixed at a reasonable level, that the number of employees is reduced to a reasonable figure, and that in all other matters curtailment of expenses is secured by economical operation on business lines.

Before the war the German railways spent 70 marks for every 100 marks which they earned. In technical railway language the "operating ratio" was 70%. This was an unusually high ratio, especially having regard to the fact that the railways paid no taxes. It was a good deal higher than the English ratio, much higher than the ratio in France. But in every country there has been since the war, a marked increase in the ratio, and we do not think that under post-war conditions the German railways can be expected to operate at a ratio so low as 70%. Not only have they now to bear the transport tax, but, though a great rise in wages—the main cause of the rise of the operating ratio in other countries—is not to be expected in Germany, the increased cost of materials, coal and steel particularly, seems likely to be permanent. We think however that an operating ratio of 80% ought to be attainable. We base this opinion in the first place on our investigation of German conditions, and especially on two facts:

(1) that new rolling stock has been acquired in the last few years in such large measure that the need of repairs and renewals will be exceptionally small for some years to come, and

(2) that the recent very large expenditure on fitting the freight wagons with continuous brakes should result in important operating economies.

In the second place, we think our knowledge of what has happened and is happening in other comparable countries justifies us in asserting in broad terms that, given efficient and economical management, there is no apparent reason why the operating ratio should not be brought back in a short time to 80% in Germany as it has already been brought back elsewhere.

In England and America, as we have said, the wages of the staff have doubled, but the tariffs are only roughly 50% above the pre-war tariffs. In the result, the operating ratio has become much higher than before and stands at present at about 80%. But the remaining 20%, calculated on a greatly increased gross revenue, suffices to give a return of over 4% on the railway capital.

Now in Germany a gross revenue of 4,000 million g. m. per annum is in sight at the present moment. With a gross revenue of 4,000 million g. m. per annum and an operating ratio of 80%, the net revenue would be 800 million g. m. And this sum added to the 227 million g. m. of the transport tax yields a total of over one milliard g. m.

And the whole of this sum can be made available for Reparation. The fall of the mark has wiped out the pre-war railway debt; the plan before the Committee will, we understand, relieve the railways under the new management of responsibility for the debts recently incurred; and capital has been so lavishly spent in the last few years that there can be no justification for further expenditure for some years to come. In future years we assume that, under commercial management, new capital will not be spent, unless with the assurance that the resulting profits or economies will at least suffice to meet the interest.

We shall revert to the matter of receipts and expenditure when we come to discuss the budget estimate for the year commencing April, 1924.

Meanwhile it may be useful to approach the subject from another point of view.

One milliard is less than 4% on the railway capital of 26 milliards. If we deduct the transport tax, which certainly does not exceed in amount the taxation levied on railways in other countries, the German railways are only required to earn a fraction over 3% on their capital. And as already stated, we have no reason to think that the German railways are over-capitalized. 3% can hardly be regarded as an excessive rate of interest.

In England the Rates Tribunal is required by Statute to permit the railways, provided that their management is efficient and economical, to charge rates adequate to produce net income of roundly one milliard g. m. on a capital somewhat less than that of the German railways. In America, the Interstate Commerce Commission, also acting under statutory authority, has decided that 5¾% is a reasonable return on railway capital, and has authorized rates regarded as sufficient to produce this return.

If the German railways are required to pay very little more than 3% for reparations, they ought, under efficient and economical commercial management, to earn a substantial surplus over and above, which can be applied in relief of the general taxation of the country. At the same time, it should be understood that the profits on railways, like those of other commercial undertakings, vary from year to year. There are good times and bad times. The milliard which we have assumed as a reasonable return must be regarded as an average one year with another.

As we have already said the full net revenue will not be attained from the outset. A period of some years will probably need to elapse. For the German traffic has been

seriously affected by the occupation of the Rhine-Ruhr railways.

Time will be needed after the railways have been reorganized as a united system to bring the new system into work and to re-establish completely the old traffic. And this reorganization will mean expenditure. Further, the necessary reform of the management will take time to carry out and will not produce its full effect at once.

For all these reasons and naturally without committing ourselves to mathematical accuracy we think it reasonable to estimate that the net revenue apart from the transport tax, and after providing for building up of an adequate reserve, will increase as follows:

1st year .....400 million gold marks
2nd year .....550 million gold marks
3rd and 4th years.....700 to 750 million gold marks
5th and subsequent years.....800 million gold marks

MEASURES TO OBTAIN RESULTS

It is evident in the first place, that the railways in common with every other German undertaking, can only give satisfactory results if the currency is stabilized and political and social tranquillity prevails.

As for the measures to be taken to obtain the results indicated above, we may repeat: the railways must be worked as a commercial enterprise, that is to say, with the determination on the one hand so to fix the rates as to produce all the receipts that can be obtained, and on the other hand to reduce the expenditure to a minimum. The management of the German railways has hitherto been far from working to this standard. We shall show later that since the war the tariffs both for passenger and freight have been kept too low, with the object of encouraging industry and commerce, and especially of favouring Ger-

man export. The tariffs are still regarded as they were before the war, primarily as a weapon in the hands of German trade, and only secondarily as a source of railway revenue.

On the other hand, the expenditure on rolling stock and works of every kind has been extravagant since the war, and the staff employed is at the same time much too large and badly paid.

It is therefore indispensable to make a radical change in the policy followed by the railways hitherto. But we do not believe that any German management will have the strength necessary to fight successfully against the traditional mental attitude, unless there is behind it the constant pressure of an expert control, established and maintained in the interests of the Allies, to supervise the management in the matter both of tariffs and of expenditure.

We shall deal later with the question of the Control in greater detail.

Further, we regard a complete change in the organization as essential. We think that the recent establishment of a separate undertaking, with a separate budget and with a certain measure of independence, though it is a move in the right direction, does not go far enough. The undertaking, though separate, still remains a Government undertaking. In our judgment it is necessary to go further and, while leaving to Germany the ownership of the railways, to entrust the management for a period of years to a commercial company, which will be German, but with a board of directors containing representatives both of the share holders and of the creditor Allied Powers.

What this period of years should be, how the company should be constituted, with what powers, and with what restrictions, is a matter which we understand the Commit-

tee itself will deal with. We need only urge that the Company and its management must have adequate freedom in the matter both of tariffs and operation. And if we may vary the phrase of Dr. Sarter, we think that a commercially managed railway company ought to treat the attainment of an adequate net revenue as of primary importance, while at the same time having regard to the progressive development of the economic life of the country, and being careful not to kill or even impair the productive capacity of the goose that lays the golden eggs.

Moreover, as we have already said, the financial result which we have mentioned can only be attained on condition that the entire German railways are either united in one system under a single management, or divided in a reasonable manner into several systems working in harmony, with the same tariffs and under the same general regulations. If we had to contemplate separate systems wholly out of harmony with each other, the results obtained would certainly not correspond to our estimate of the net revenue obtainable.

Though that estimate assumes the existence of an undivided German railway system, it will of course be understood that, in making this assumption we do not express any opinion as to the course of action which the Allied Governments may think it desirable to adopt or on the general question of military or economic guarantees for reparation and security.

Finally, our estimate takes for granted that the railways will not be required to carry traffic for the Government or the community, unless their services are paid for at a commercial rate. Hitherto the German railways have carried free for the Post Office not only mails but parcel traffic. The railways of Great Britain receive at the present time from the Post Office payments for similar though

smaller services amounting to more than four million pounds sterling per annum. There are other instances of a similar kind but of less importance with which it is not necessary to deal here.

FUTURE CAPITAL EXPENDITURE

We shall see later that the expenditure incurred since the war for new works, and especially for rolling stock has been very large. It has in our judgment gone much beyond the real needs of the railways.

For rolling stock alone there has been charged against the various budgets, a sum of more than 3 milliard gold marks, which has enabled the railways to acquire more than 18,000 new locomotives and more than 400,000 new carriages and wagons.

We think therefore that, broadly speaking, the capital account can be entirely closed for some years to come, without any injury to the railways. But at the same time we must not fail to call attention to the statement of the German Government that the capital expenditure to be incurred in the year 1924 will amount to over 500 million gold marks, and that to complete the programme a further expenditure of 236 million gold marks will be required in 1925. We think that this programme ought to be examined in detail, and very drastically cut down.

Still, after a certain time it will no doubt be necessary to incur new expenditure in enlarging stations or building new lines. But as we have already said, a commercial administration will not embark on new capital expenditure unless it is evident that it will be directly reproductive. The cost can therefore be paid either directly, out of increased net revenue, or if it is sufficiently important to justify this course, by loans charged on the increased revenue without trenching on the revenue pledged for reparations.

THE RAILWAY BUDGET—ORDINARY BUDGET

It seems desirable to examine the estimate for the ordinary budget for the financial year from April 1, 1924 to March 31, 1925—in German financial matters called the year 1924—which has been drawn up by the German administration.

It has been drawn upon the supposition that the Rhine-Westphalian Railways have been restored to German management. But even if and when this happens, it is probable that there will be confusion at the outset; a certain time must necessarily elapse before the normal working can be resumed and the ordinary currents of traffic restored; and further, certain exceptional expenses will have to be incurred which it is impossible to estimate exactly.

This budget is therefore somewhat theoretical, and may be considered as representing the results to be obtained in the year 1925 rather than in the year 1924. Subject to these reservations, we will proceed to summarize and examine it.

Ordinary Budget Including the Rhine-Westphalian Railways

I. EXPENSES.			
a. Salaries and Wages			1,631,007,000 gold marks
b. Cost of Material:			
Supplies and consumable stores	545,000,000		
Maintenance of way and works	294,480,000		
Maintenance and renewal of rolling stock and mechanical plant	394,000,000		
Other material costs	140,513,000		
Reserves	200,000,000		
Interest and repayment of debt	325,000,000		
		1,898,993,000	
Total		3,530,000,000	
II. RECEIPTS.			
Passenger traffic		850,000,000	gold marks
Freight traffic		2,700,000,000	
Miscellaneous		130,000,000	
Total		3,680,000,000	
Surplus		150,000,000	

Receipts

The receipts for the budget in 1924 have been calculated by assuming a traffic somewhat greater than that in 1913, but less than that in 1921 and 1922, in which years the traffic was swelled by the activity of trade due to the fall of the mark.

The figures are as follows:

	Actual in 1913	Estimate for 1924
Passenger kilometres	35,122 millions	40,000 millions
Ton kilometres	57,251 millions	60,000 millions

The passenger receipts have been calculated on the basis of the tariffs which were in force at the time when the budget was framed. Later on, when we come to deal with tariffs, we shall point out that the 3rd and 4th class fares were too low, and that the 1st class fares which affect only a trifling number of passengers, were too high. Since March 1st the 3rd and 4th class fares have been increased by 36%, and the 1st class fares have been slightly reduced. We may assume that the result will be an increase in passenger receipts of 30%, which will raise the budget estimate of 850 million to roughly 1,100 million marks.

The freight receipts have been calculated on the basis of an average charge of 4.5 gold pfennigs per ton kilometre. The tariffs in force last February, at the time of our visit to Berlin, gave a higher average receipt per ton kilometre of 5.5 gold pfennigs. But a general reduction of 10% was made on March 1st, and others are in contemplation with the special object of encouraging national trade and industry. As we shall explain later, these reductions do not seem to us justified under present conditions. If rates were maintained at a reasonable level, we may assume that the freight receipts would be about 10% above the budget estimate of 2,700 million marks, that is, they

would amount to 2,970 million marks. The receipts side of the budget would then be as follows:

	Million Gold Marks
Passenger traffic	1,100
Freight traffic	2,970
Miscellaneous	130
Total	4,200

EXPENSES

As for the estimate of expenses for 1924, it is to be noted that the expenditure for staff, 1,631,007,000 gold marks, represents about 54% of the actual working expenditure of 3,005 million gold marks. If we exclude interest and repayment of debt, and reserve, neither of which are properly included in working expenses, this proportion is much the same as that on the railways of the adjacent countries. We pointed out in previous Notes that the staff was unreasonably large. In 1919 there were 1,121,111 permanent staff and workmen employed; at the end of 1923 the number was still very nearly one million. They must have been extraordinarily badly paid, for the percentage of the wage bill to the total expenditure was reduced in the budgets of 1922 and 1923 to 29% and 20% respectively, a figure absolutely abnormal.

The expenditure for 1924 has been calculated on the basis of a staff reduced to 793,000 although on the 1st of January the number was still 936,800. A very drastic reduction is therefore implied, and is in fact being carried through at this moment. But there will be no saving in money. Increase of wages will more than counterbalance the decrease in the number of staff, for an increase of salaries and wages amounting to 18% on the average is budgeted for. A table of the variations in the average payment is given below:

Average payment per employee per annum in gold marks

	Year 1914	Feb. 1924	Budget Estimate for 1924
Permanent staff	2,352	1,634	1,972
Workmen	1,331	1,060	1,338
Average	1,718	1,293	1,595
Percentage of pre-war average	100%	75%	93%

We feel bound to say that the increase proposed is entirely reasonable. The remuneration of the staff, especially in the upper and middle ranks, is quite inadequate, and if good work is expected, it must be paid at its market rate.

A reserve of 200 million marks has been included to provide for contingencies, a course which we cannot other than approve.

The total expenses for the year 1924, including this reserve and interest and repayment of debt, to which we shall refer later are set down in the budget as..... 3,530 million gold marks
With the tariffs on the basis which we have taken above, the receipts will be..... 4,200 million gold marks

This would give a surplus of 670 million gold marks
This surplus would be net profit because the reserve of 200 million and 325 million gold marks for interest and repayment of the new debt has been included in the expenses.

Further it is to be remembered that the transport tax represents in effect a further net profit from the railways. If we reckoned this tax at 10% on the passenger receipts and at 7% on the receipts from freight other than coal, we should obtain for 1924 a figure of 276 million gold marks.

The total net income of the railways would then be 670+276=946 million marks, which is very close to the milliard which we have suggested is attainable within a few years.

But as we have said already, these results are applicable to the entire German railways worked as a single system, including the Rhine-Westphalian lines, under normal conditions. Certainly they will not be obtained in the year 1924, though they should be obtained very shortly thereafter.

Interest and Repayment of Debt

The sum of 325 millions set down in the budget for interest and repayment of debt during the year 1924 is divided into:

	Million gold marks
Interest	99
Repayment	225
Cost of Administration	1
	325

This debt represents liabilities recently incurred, for the old debt has practically disappeared. The total amount of the current debt is 312 million marks. Particulars are given in the reply of the Government to questions asked by the Committee. There are short term loans, overdue accounts, bills of exchange maturing, advances made by the Ministry of Finance or by the Reichsbank, and emergency currency issued by the railways which has to be redeemed. The interest charge for these debts is quite large. In certain cases we are told that interest is running at the rate of one-tenth of 1% per diem, that is 36% per annum. Evidently debts of this kind should be paid off as soon as possible.

In addition to these current debts amounting to 312 millions, it is estimated that further debt will need to be incurred as follows:

	Million gold marks
Commitments for extraordinary expenses up to March 31, 1924	110
For the expenditure of the extraordinary budget during the financial year 1924	387
For expenditure which will be necessary when the Rhine-Westphalian Railways are handed back	200
	697
Add debt already incurred	312
Total debt, actual and anticipated	1,009

As we have said, the ordinary budget for 1924 provides an amount of 225 million marks for repayment of debt. But it is evident that these expenditures charged on the extraordinary budget tend to increase rapidly, and it is therefore necessary to cut down the extraordinary budget. To this question we now turn.

THE EXTRAORDINARY BUDGET

A budget of extraordinary expenditure has been drawn up for the interim period from November 15th, 1923, to March 31st, 1924. It covered originally an expenditure of 220 million, but was subsequently reduced to 170 million marks divided as follows:

	Million gold marks
CHAPTER I	
Dwellings	8
Additional rolling stock	77
Kunze Knorr brake	3
Miscellaneous	15
CHAPTER II	
Doubling of road	6
Electrification	6
Stations	32
Repair shops	13
Miscellaneous	10
Total	170

These expenses are to be covered partly by credits already available, and partly by new credits to an amount of 110 millions.

The Ministry has also furnished us with a statement of other extraordinary expenses which in their judgment are still necessary for the financial year 1924. We summarize them as follows:

CHAPTER I

	Million gold marks
Dwellings	15
Additional rolling stock	110
Electric rolling stock	20
Kunze Knorr brake	28
Miscellaneous	40

CHAPTER II

New tracks	10
Doubling of road	13
Electrification	10
Stations	94
Repair shops	36
Miscellaneous	11
Total	387

In addition to this expenditure of 387 million marks in 1924, it is estimated that a further sum of 236 millions will subsequently be required merely to complete works already begun. This represents the final state of a programme amounting altogether to 1,610 million marks.

This estimated expenditure, which will have to be covered by loans, has, so we are told, already been reduced to an absolute minimum. All the same, we think it ought to be reexamined point by point in order to stop or at least postpone work not absolutely necessary, except where it has been carried to such a point that it had better be completed.

The works and the rolling stock of the German rail-

ways were very fully adequate before the war. Since the war no money has been spared to enlarge works and buildings and to renew and even increase the rolling stock to an extent which will make it impossible to justify any new expenditure of this nature for some years to come. We give below particulars as to the rolling stock which bear out this statement.

ROLLING STOCK

Below is a comparison based on figures furnished to us in Berlin, of the German railway rolling stock before the war and in 1924. We have ignored electric locomotives and motor cars:

	Steam locomotives	Carriages	Wagons
End of 1913	27,940	62,050	657,150
January 1924	29,966	67,800	723,100

Further rolling stock ordered last year from private firms and not yet delivered amounts to:

Locomotives	Carriages	Wagons
884	1,453	25,653

Delivery of this stock was due by the beginning of May, but has been delayed owing to the occupation of the Ruhr. It is not now expected to be complete till the end of the year.

These figures show that the whole of the rolling stock handed over, either at the Armistice or together with the territory ceded under the Treaty of Peace, has been replaced by new; old and out-of-date rolling stock, which could only be replaced to a very small extent during the war, has been written off and replaced since 1920; a considerable quantity of additional rolling stock has been built.

It is worth while producing a table showing the locomotives written off and replaced for each year of the last eleven:—

In 1913	there	were	written	off	.....	600	locomotives
In 1914	"	"	"	"	.....	379	"
In 1915	"	"	"	"	.....	253	"
In 1916	"	"	"	"	.....	237	"
In 1917	"	"	"	"	.....	220	"
In 1918	"	"	"	"	.....	167	"
In 1919	"	"	"	"	.....	191	"
In 1920	"	"	"	"	.....	690	"
In 1921	"	"	"	"	.....	1,849	"
In 1922	"	"	"	"	.....	1,585	"
In 1923	"	"	"	"	.....	1,500	"
Total					.....	7,671	"

The same thing has happened with carriages and wagons. We give a table showing the new rolling stock acquired since 1914:

	Steam locomotives	Carriages	Wagons
Delivered: 1914-1918	8,859	11,832	181,196
Delivered: 1919-1923	8,506	12,313	246,388
Ordered but not yet delivered..	884	1,453	25,653
	18,249	25,598	453,237

The result is that 18,249 locomotives and 478,835 carriages and wagons, two-thirds of the entire stock, have been built within the last ten years; and that accordingly the rolling stock of the German railways is much superior to that which they possessed in 1914.

Replacement of rolling stock on this colossal scale has necessarily entailed enormous expenditure. We are unable to give the actual cost, for it is spread over various budgets.

The figures which have been given to us show an expenditure, up to the end of 1922 only, of 2,267,774,488 marks.

This figure does not include the cost of replacing the rolling stock handed over to the Allied Powers in 1919, 1920 and 1921, which was paid for by special credit

granted by the Ministry of Finance, amounting when reduced to gold marks to 739,347,006.

The replacement of rolling stock written off is charged against the ordinary railway budget. Additions to rolling stock are charged against the extraordinary railway budget.

From November 15, 1923, to April 1, 1924, rolling stock to an amount of 150 million gold marks will be so charged.

A further expenditure of 50 million marks in the ordinary budget and of 110 million marks in the extraordinary budget is proposed for the year 1924.

KUNZE KNORR CONTINUOUS BRAKE

The application of the Kunze Knorr continuous brake to freight trains has also implied large expenditure. It was decided in 1918, while the war was still going on, to adopt this policy in order to release a large number of brakesmen, and to make possible an increase of speed of freight trains, more especially of military trains. This policy has been energetically pursued since the war; on the one hand, all the new wagons ordered have been fitted with continuous brakes, and on the other hand, the equipment of the old stock has been pushed on.

The entire programme is expected to be completed by April 1, 1925. The total expenditure will amount to 400 million marks, of which 117 millions still remain to be paid. But it should be said that the Kunze Knorr Company has agreed to spread the payment over a period terminating only on October 1, 1926.

TARIFFS

FREIGHT TARIFFS

A study of the freight tariffs of any country at any time involves prolonged investigation of a vast mass of bewildering detail. To present in brief outline the broad

general effect is almost impossible. Certainly the short time available has not made the task possible for us. In Germany its difficulty is increased by various special circumstances.

In 1921 the whole basis of the freight tariffs was altered by the abandonment for a large part of the traffic of flat mileage rates, and the substitution therefor of *Stafeltarife*, that is, rates under which the charge per mile decreases as the mileage increases. Simultaneously, most of the exceptional tariffs, under which the bulk of the traffic had hitherto passed, were withdrawn. Many of them have since been restored in a modified form. And this is only the railway side of the difficulty.

The currency question complicates the whole story. Tariff advances were at the outset made in the shape of percentage increases of existing rates. Then came a period when an index figure was adopted with a varying multiplicator. Finally in November, 1923, the tariffs were calculated on a gold basis. The result, as we are informed, was that the freight tariffs were found to be on a level so high in comparison with the capacity of the traffic to bear the rates, that reductions on a large scale became absolutely necessary.

We are far from satisfied that this was or is the case. We feel convinced that further investigation would support our general conclusions that the freight rates have been, and are proposed to be, reduced in a manner and to an extent which cannot be justified from the railway point of view, and that this has resulted from the training and mental attitude of the officials, who have been brought up to share the views expressed in the quotation from Dr. Sarter which we have given above.

At the same time we feel it necessary to utter a note of warning. Our conclusion, that freight tariffs might be a good deal higher than the German officials think they can

profitably be, is based mainly on the average receipts per ton-kilometre to-day as compared with the pre-war figures. We are told that these figures give a misleading impression of present-day facts. And numerous comparisons of certain important rates and classes of rates, pre-war and post-war, have been submitted to us, which would, if typical, put a different complexion on the matter. In spite of these tables we still adhere to the opinion we have expressed. But the Committee will appreciate that what we have said is only an expression of opinion, and cannot claim to be a considered judgment based on fully ascertained statistical facts.

We have found it impossible to satisfy ourselves how high the present German freight tariffs really are. The earliest documents submitted to us stated that the freight tariffs might be assumed to be double the pre-war tariffs. The facts do not seem to us to bear out this statement. Before the war the freight charge per ton-kilometre averaged 3.36 gold pfennigs. It is estimated by the officials that in November, 1923, at the moment when the gold mark was substituted for paper marks of indefinite value as the medium of payment for railway services, the average rate was double the pre-war. In other words, according to the official estimate, the average rate in November, 1923, should have been 6.72 pfennigs per ton-kilometre. But this is no more than an estimate, and we doubt its accuracy.

From this date there began a process which is still continuing of repeated and important reduction of rates regarded as excessive. There is statistical ground for believing that in the early part of January, 1924, the average rate was 5.89 pfennigs, an advance, that is, not of 100% but of 75% above the pre-war average. On January 20th a number of important reductions came into force, and the estimate, based on such statistics as were available, was in

the middle of February that the then average rate was 5.55 pfennigs, an advance on pre-war rates of 65%. The reductions are however still going on, and some of them are of great importance. On March 1st an all round reduction of 10% was made on a large part of the traffic.

The budget estimate of freight traffic receipts is made on the assumption that the average freight rate during the year will have been brought down to not more than 4.50 gold pfennigs, which is equivalent to an advance over the pre-war tariffs of only 33%. No doubt this estimate errs, as was intended, on the side of caution.

On this policy we will make two observations. Taken as a whole, we have difficulty in believing that all particular reductions made and proposed can be justified. Even assuming that in certain cases reductions have been and are desirable in the interest of the railways, we feel convinced that reductions are being conceded which need not be made, and that at least in some cases the percentage of reduction is unnecessarily large. We have learned that exceptional tariffs involving great reductions, both for import of raw materials and for export of German produce, are being very freely introduced. The import rates for jute have been reduced by 25%; for raw cotton and raw wool by 50%. A reduction of the rate for miscellaneous wares exported by sea, amounting to 30%, is on the point of coming into force; and a reduction of 30% to 40% in the rates for steel and iron exported by sea is contemplated.

There is a point in connection with the freight tariffs and freight revenues which, though the precise facts are obscure, is of considerable importance. The Budget estimate for 1924 assumes, apparently with good reason, that the ton-kilometres to be carried in 1924 will be roughly equal to those of 1913. But conditions have greatly changed in the interval. The number of tons carried has

fallen apparently by about 20%, while the distance the average ton travels has increased in corresponding ratio. The German officials adduce three main causes for the increase in the average length of haul:

(1) The introduction in 1921 of *Stafeltarife;*

(2) Changes in the previous currents of traffic consequent on the war and the establishment of new political frontiers;

(3) Diversion of traffic in consequence of the occupation of the Rhine-Ruhr territory.

The effect of (1) will be permanent; the effect of (2) will probably diminish with time; the effect of (3) will presumably be only temporary. We cannot estimate what proportion of the ascertained results has been due to these three causes respectively. But it is clear that, if in future years the tonnage does not increase, while the average length of haul goes back to anything approaching the pre-war figure, the effect on the railway revenue will be quite serious.

Before we leave the question of freight tariffs, we desire to make one observation. We have admitted that the facts are obscure; that our investigations have not been and could not be pushed very far. We have acknowledged that we have hesitated as to certain conclusions. It may well be that, where we have expressed a definite opinion, time will prove the opinion wrong.

All this we have had in mind; it does not affect the thing which from the point of view of the Committee is the really important matter, that we retain the conviction that the German railways can and should produce a net revenue of one milliard gold-marks per annum available for reparation. Our forecast may well prove erroneous on certain points, too optimistic in one direction, too pessimistic in others. But our estimate is based on broader grounds than tariff details and to it we adhere.

PASSENGER TARIFFS

The German railways have nominally four classes of passengers; but first-class carriages are not run on local trains, and fourth-class carriages are not run on express trains. The fares before the war were respectively at 7 pfennigs, 4.5 pfennigs, 3 pfennigs and 2 pfennigs per kilometre. In April, 1917, the transport tax, amounting to 16%, 14%, 12% and 10% on the gross receipts from the four classes respectively was introduced.

In spite of the tax, which is estimated to amount for 1924 to 85 million gold-marks, the railway management did not raise fares till September, 1923. At this date the fares were increased, including tax, to 19.6 pf., 9.9 pf., 3.3 pf. and 2.2 pf. per kilometre, for the 4 classes respectively. Therefore the 3rd and 4th class fares were only increased by the amount of the tax, while the 1st and 2nd class fares were more than doubled. The result of fares so obviously out of proportion was to empty the higher classes. Accordingly in December last, the 1st and 2nd class fares were reduced by one-third. But even then, the 1st class fare was four times the 3rd class, and six times the 4th class. Naturally the 1st class was absolutely empty, being used by seven passengers out of 10,000, while seven passengers out of 100 traveled 2nd class. A good deal more than half the passengers travel in the 4th class, and a good deal more than one-third in the 3rd class. Seeing that a 3rd class passenger could till a few weeks ago travel 30 kilometres, and a 4th class passenger 45, for one gold mark with an ordinary ticket, and that more than half the total number of passengers in fact travel with season tickets issued at a rate roughly one-half of the ordinary rate—could travel, that is, respectively 60 and 90 kilometres for one mark—it is not surprising to find it admitted that the rates for passenger traffic have been quite insufficient to cover the

working expenses. At length, as from the 1st of March, while the 1st class fares have been further reduced to a level which may possibly secure a few additional 1st class passengers, the 3rd and 4th class fares have been increased by 36%. The fares of the four classes are now 9 pf., 6 pf., 4.5 pf., and 3 pf., per kilometre, and the ratio between the classes is less unreasonable than hitherto.

We can hardly think that these new fares will be unduly burdensome to the German public, seeing that the German 3rd class fares per kilometre will still be only half the corresponding fare either in England or in the United States. But the public have so long been accustomed to be carried at non-commercial rates that we think some falling off of traffic is to be expected, at least at the outset. We have accordingly estimated that a 36% increase in fare will only produce a 30% increase in receipts.

FUTURE CONTROL—THE RAILWAY COMMISSIONER

It is evident from the facts and figures set out above, that the German Government has since the war run the railways in a manner which cannot be defended. On the receipts side it has failed to raise the revenue which might have been and ought to have been raised. On the expenditure side it has spent capital not merely on restoring the pre-war situation, but on betterments of all kinds which under the existing conditions cannot be justified. The railways have not merely been restored to their pre-war state of efficiency, but have been brought up to a much higher standard, a standard which to the best of our knowledge is superior to that of any other country. We are given to understand that even inside the Ministry itself this policy has been severely criticised. The excuse is that

the pressure on the one hand of the great manufacturers to keep their works going and to avoid a wholesale dismissal of employees, which might lead to revolts or even revolution, was too strong to be resisted; while on the other side, the poverty of the mass of the population was so great that the Government was compelled to maintain railway rates at a low level. Whatever may have been the reason, there can be no doubt of the facts.

Our own view is that, while the reasons above had considerable weight, the action taken was by no means wholly due to external pressure. The officials in the tariff section of the Ministry were, as we have repeatedly said, only too ready to subordinate railway interests to non-railway circumstances. And the executive officers, whether charged with engineering or traffic management, were afflicted with what it is not too strong to describe as megalomania. They regarded it as due to the dignity of the German Reich that buildings should be magnificent, that railway plant should be up to a very high standard, that such and such services should be given, and so on. They had never been taught the commercial necessity of cutting their coat according to their cloth.

Now the mere transference of the railways from State to Company management will not of itself alter this mental attitude. A large part of the Board will be German; the General Manager will be German; and his responsible officials will be the same men who have inspired and carried out the railway policy of the past. We think it therefore essential that a Railway Commissioner should be appointed by and on behalf of the Allies to supervise and, if it should hereafter become necessary, to control in their interest the German management. We will therefore, in concluding this Report, deal with what in our opinion should be the functions of the Railway Commissioner and the organization of his staff.

THE RAILWAY COMMISSIONER

The Railway Commissioner must be a person who is acknowledged in the railway world as being in the first rank. It must be left for him, when appointed, to say what assistance he needs, in order to be able to assume responsibility for control of all branches of railway management. It will be his duty also to consider how far it is necessary to have local representatives in any or each of the districts into which the German railway system may hereafter be divided.

We assume that when appointed he will produce to the Board an outline of the organization and the staff that he regards as necessary, and it will be for the Board to approve his scheme. He must have the right to receive of course all reports, statistical and financial returns, proposals for extra-routine expenditure, whether on capital or revenue account, for changes in tariffs or for the concession of exceptional rates and the like, when they are of such importance as would normally require the sanction of the General Manager. He must also have the right to call for any further reports, returns and statistics, as he may think necessary, in order to enable him to form an independent judgment.

Being in possession of full and up to date information as to everything that is happening or is proposed, his first duty will be to decide whether to approve or disapprove. If he disapproves, or even hesitates to approve, he will discuss the matter with the General Manager. He may be of opinion that things are going wrong, or that a course of action inconsistent with the railways being able to earn a financial return is likely to be adopted. In such a case it will be his duty, if he fails to induce the General Manager to modify his policy, to bring the matter to the attention of the Board in order that they may be in a position to

take such action as they think fit. It is to be hoped that, if the right man is appointed to the post, he will be able to work in entire harmony with the General Manager; and that the General Manager, so far from resenting his interference, will welcome his support in putting a stop on the one hand to unnecessary expenditure, and in enforcing on the other hand the establishment and the maintenance of tariffs proper and adequate to secure for the railways as much net revenue as can reasonably be obtained without unduly hampering the trade of the country.

A second function of the Commissioner will naturally be to make for the foreign members of the Board reports on any points which they may regard as of serious importance. We may suggest the reasonableness of the greatly reduced German export tariffs as a sample of this class of question. It is clear that the Allied Nations have a right to claim that the net revenue of the German railways should not be reduced in order to give to German manufactures an unreasonable advantage in overseas markets.

It does not seem necessary to discuss in detail what would be the position of the Commissioner if the German railways failed to yield the net revenue fixed as reasonable for reparation purposes. We assume that, broadly speaking, in this case the Commissioner General will take over the functions of the General Manager, and that, in lieu of discussing with the General Manager or recommending to the Board of Directors, he would be empowered to issue positive orders, whether for stopping expenditure which he considered unjustifiable or for an increase which he considered reasonable in existing tariffs. It is evident that it would be necessary to require the German Government to agree in advance that, if payment on the agreed scale failed to be reached or even if there was serious danger that this failure would occur in the immediate future, the

Commissioner, as the representative of the Allies, should be entitled to enter into full control.

Signed: W. M. Acworth.
G. Leverve.

ANNEX NO. 4 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

CONCESSION OF THE WORKING OF THE RAILWAYS

The working of the German railways shall be legally transferred to a company by a fixed date. The law will ratify the contract to be entered into between the German Government and the company to which the concession is made. The contract will provide that no change can be made in the conditions of the concession without the consent of the company and the trustee for the bondholders referred to below.

The law will further provide that the company shall have a monopoly of all railway extension in Germany.

The charter of the company will be annexed to and approved by this law. Before being submitted to the German Parliament the law will have to be approved by the Reparation Commission.

The conditions under which the working of the German railway system will be transferred to the Company by this law, shall be as set forth below.

The Company will be of German nationality.

The Company shall be responsible for the working, upkeep and normal development of the railways, including rolling stock and equipment, and will be entitled, subject to the provisions hereinafter contained as to the powers of the German Government and the Railway Commissioner, to conduct its business in such manner as the company may think proper.

The German Government shall have such control over the tariffs and service of the railways as may be necessary to prevent discrimination and to protect the public, but such control shall never be exercised so as to impair the ability of the railroad Company to earn a fair and reasonable return on its capital value, including adequate provision for its bonds and preferred shares, a return on its ordinary shares and adequate reserves for all purposes including amortisation of capital. The plan to accomplish the foregoing shall be worked out by the Organization Committee hereinafter referred to.

The Company shall as from the commencement of the concession be entitled to charge the tariffs then in force. Thereafter the Company shall be entitled to vary the tariffs or any of them from time to time, subject to the provisions of Articles 365 and 378 of the Treaty of Versailles.

It shall be the duty of the Organization Committee to settle the manner in which, subject always to the preceding provision, the control of the German Government over the service and the tariffs shall be exercised.

The term of the concession shall be at least of sufficient length to allow of the amortisation of the bonds according to the provisions hereinafter contained. On the expiration of the concession, the company shall return to the German Government free from all charge, the whole of the railway undertaking, including all rolling stock and equipment, in thoroughly good and complete working order.

As the consent of the German States is necessary under the German Law of 1920 for any alienation of or charge upon the German railways, the German Government shall make in this respect all necessary arrangements with the States concerned. These arrangements shall be ratified by the law granting the concession.

This law shall confer upon the Company the right to mortgage any property belonging to the railways.

It shall also contain an undertaking that neither the Reich nor the States nor any public authority shall impose on the Railway Company any new direct tax, whether upon receipts either gross or net, or upon movable or immovable property or in respect of the employees of the company or otherwise howsoever.

THE RAILWAY COMPANY

Article I

CAPITAL OF THE COMPANY

The total capital which will be created, added to the first mortgage bonds for eleven (11) milliard marks gold referred to below, will correspond to the capital cost of the German railway system (26 milliard marks gold).

Preference shares will be created to the amount of 2 milliard gold marks, bearing a fixed rate of dividend and entitled to participation in the profits of the railways, after payment of the annual payments mentioned below. This dividend and this participation as also the terms on which the German Government may pay off or re-purchase these shares, will be fixed by agreement between the German Government and the Organization Committee described below.

These preference shares will be sold by the Company for the profit of the German Government and of the Company itself, one-fourth (¼) of the sum thus obtained will be the property of the German Government and three-fourths (¾) the property of the Company. The sales of shares will be made under such conditions that the German Government will receive the whole sum due to it with-

in two years. If the German Government so requires, the proceeds of the first sale of shares may be reserved for its use.

The balance of the capital cost of the German railway system (viz. 13 milliard gold marks) will be represented by ordinary shares, to be owned by the German Government and to be kept or sold by it as it prefers.

Article II

ADMINISTRATION AND MANAGEMENT

The Company will be administered by a Board of Directors of at least eighteen (18) members, who shall all be business men of experience or railway experts. Half (½) of these will be appointed by the German Government and half by the Trustee referred to below.

As soon as preference shares are issued to the public, the holders of these shares shall be entitled to elect four members of the Board in place of four members appointed by the German Government.

The Organization Committee will also fix the duration of the term of office of the Directors of each class.

Of the nine (9) members of the Board of Directors appointed by the Trustee, five (5) may be German nationals.

The Chairman of the Board will be elected for one year by a three-fourths (¾) majority of the members of the Board and will be eligible for re-election as long as he possesses the necessary qualifications.

As soon as the preference shareholders shall elect directors, the Chairman shall be chosen from the directors so elected.

He will in addition to his vote as a member of the Board, have a second or casting vote.

The General Manager of the Company shall be of German nationality.

He will not be eligible for a seat on the Board. He will be appointed by a three-fourths (¾) majority vote of the Board.

He may be removed by the same majority. If however his removal is requested by the Commissioner (provided for in Article III below) on account of violation of the Charter of the Company or of failure to comply with the instructions of the Board of Directors, he may be removed by a simple majority vote of the Board.

Whatever decisions may be taken with regard to the operation of the railways, it must be understood that any breaking up of the working of the system into local divisions must not in any event affect the financial and tariff unity of the undertaking.

Article III

COMMISSIONER

The Railway Commissioner shall be a person accepted in the railway world as being in the front rank.

He shall be appointed by a majority vote of the foreign members of the Board of Directors.

He shall not be a member of the Board.

He will have an adequate staff of experts in railway matters and in accountancy.

The Commissioner will have a general right of inspection over the whole railway system and all the railway installations and subdivisions, either in person or by deputy.

He shall also be entitled to receive all reports, statistical and financial returns, proposals for extra-routine expenditure whether on "capital" or "revenue" account, for changes in tariffs or for the concession of exceptional rates, and the like, which are of such a nature as would normally require the sanction of the General Manager.

The Railway Commissioner will further be entitled to

call for any other reports, returns, or statistics which he may consider necessary in order to enable him to form an independent opinion. All this information shall be furnished promptly, fully, and accurately at his request. If any measure in connection with construction, operation, or tariffs tends substantially to menace the rights or interests of the bondholders or of the Reparation Commission, as defined below, and in particular to endanger the payment at the due dates, referred to in Article V below, he shall discuss the question with the General Manager. If he cannot persuade the latter to change his line of conduct, he must lay the question before the Managing Board, in order that it may take any measures it may deem necessary.

If the service of the bonds hereinafter mentioned is in jeopardy, the Commissioner shall have regard to the provisions for the security of the bondholders hereinafter contained.

The expenses of the Railway Commissioner and his staff shall be an operating charge upon the receipts of the railways.

Article IV

BONDS

The Company shall forthwith, after its creation, issue without payment and for the purpose of reparation, to a Trustee appointed by the Reparation Commission, first mortgage bonds to a nominal amount of 11 milliard gold marks carrying interest at 3% per annum for the first financial year of the Company, at 4% plus a bonus of 25 millions for the second, 5% for the third and subsequent years, and to be amortised by a sinking fund as hereinafter provided.

Payment of these bonds shall be guaranteed by the German Government and they shall be signed both on

behalf of the Company and by the Finance Minister acting on behalf of the German Government.

These bonds shall be secured by a first registered mortgage or charge on the corpus and revenues of all immovable property used by or belonging to the Company present or future, and by a first floating charge on all its fixed and movable plant, rolling stock and all installations. The Company shall be authorized by the concession to create this mortgage and charge, the duration of which shall not be limited to the period of the concession.

This mortgage and this first floating charge shall be expressed to be in favor of the Trustee to be appointed by the Reparation Commission, provided always that the Company and the German Government shall be entitled at any time, with the consent of the Trustee, to sell or dispose of any particular property used by the Railway Company which may be considered to be no longer needed by the latter, upon such terms as to the application of the proceeds of the sale as may be agreed upon by the Trustee.

The service of the bonds shall be assured by the following payments which shall be made to the Trustee from the gross receipts of the Company and before the ascertainment of any net profits; that is to say:

	million gold marks
a. for the first financial year of the Company..	350
b. for the second financial year.....	465
c. for the third financial year.....	550
d. for the fourth and subsequent financial years	660

If in any year the German railways fail to realize receipts sufficient to allow of the payments above mentioned (it being understood that the Company may draw upon whatever reserves may be available for this purpose until such reserves are exhausted), the Railway Commissioner shall have the right to take such action as the Trustee for the bondholders may consider is necessary to protect the

rights of the bondholders, including the right to operate, to lease, or to sell all or any of the railways and property subject to the mortgage or charge of the bonds.

From and after the end of the fourth year from the date of the formation of the Company, the bonds shall be amortised, under the conditions to be determined by the Trustee with the approval of the Reparation Commission, by the application in each year of such part of the annual payments above mentioned as shall not be required for the interest on the bonds.

The German Government and the Company shall also be entitled at any time to pay to the Trustee sums additional to the above payments with the authorization of the Reparation Commission which shall ascertain from the Transfer Committee that the transfer of these additional funds does not disturb the transfer of the annual payments. Any sums so paid shall be applied first to the discharge of any interest in arrear and next upon six months public notice in redeeming at par all or any part of the bonds for the time being outstanding.

The Reparation Commission shall be entitled, with a view to the mobilization of the bonds, to divide the same in any manner which it may think expedient into different classes with different rights—as to priority of charge, rate of interest, repayment of capital and otherwise—against the annual payments to be made by the Company, and to issue to the public upon such terms and generally in such manner as the Commission may think proper, bonds, debentures, debenture stock, certificates of indebtedness or other securities of any nature secured upon the whole or any part of the bonds.

The Company shall not be able to issue other bonds than those referred to above without the authorization of a three-fourths majority of the members of the Board, of which majority two must be foreigners.

All payments of interest and capital in respect of the bonds shall be free from all German taxation except in so far as the persons entitled thereto may be liable under German law to the payment of German direct taxation.

Subject as herein provided the form of the said bonds and all provisions as to the enforcement and repayment thereof including drawings and giving time for payment shall be settled by the Trustee with the approval of the Reparation Commission.

Article V

ENFORCEMENT OF GOVERNMENT GUARANTEES

If the company shall at any time make default in meeting the service of the bonds, the Trustee may in lieu of or in addition to the measures mentioned in the last preceding Article present the accrued coupons or any bonds due for repayment to the Commissioner of Controlled Revenues who shall pay them at their face value out of the portion of the receipts of the assigned revenues falling to the share of the German Government. The coupons and bonds so paid shall be included at their face value in the repayments made by the Commissioner of Controlled Revenues to the German Government. The amounts so paid may only be repaid by the Company to the Government after the necessary provision has been made for the current and the next coupons on the bonds and for the fixed dividend for the current year on the preference shares.

Article VI

TRANSPORTATION TAX

The Company shall on behalf of the Government pay to the Reparation Commission the proceeds of the transportation tax as at present levied, *i. e.*, a tax of 7% on the

gross receipts from all freight traffic other than coal, and a tax of 10% to 16% according to class, on the gross receipts from all passenger traffic. This payment shall be made during the first and each of the following years of the concession and until the conclusion of any extension, even if in the course of the concession the whole of the bonds have been paid off.

The rate of the transportation tax shall not be reduced during the whole of the concession. The proceeds of the tax may be employed by the trustee to secure the issue of a special series of bonds for 3 milliard gold marks, or thereabouts.

Article VII

FINANCIAL ARRANGEMENTS

The bank account shall be kept at the new Bank. Payments by the Company hereinbefore prescribed shall be paid to the account of the Railway Commissioner. The latter shall transfer these sums to the credit of the agent for Reparation payments.

Article VIII

ANTICIPATORY REDEMPTION OF BONDS

If all the first mortgage bonds should be redeemed before the expiration of the term of the concession by special subsidy by the German Government to the Company, the Government shall be entitled to require that the functions of the Railway Commissioner hereinbefore mentioned shall come to an end and that the foreign directors shall be replaced by German directors. In default of other arrangements, the transportation tax shall continue to be paid to the Reparation Commission.

The German Government shall in that case also have the right to purchase or repurchase the preference shares at par, plus dividend and arrears of dividend if accrued.

Article IX

ORGANIZATION COMMITTEE

A temporary Committee with the title of the "Organization Committee of the German Railway Company" shall be constituted in order to work out, subject to the foregoing provisions, the details necessary for the creation of the German railway company and the execution of this plan. The Committee shall consist of two delegates appointed by the German Minister of Railways, the railway specialists, Sir William Acworth and M. Leverve, who are familiar with the discussions which have led to the adoption of this scheme, or a nominee or nominees to be appointed by them jointly together with a fifth member of neutral nationality to be chosen by the four thus appointed or, in default of such choice, to be appointed by the Reparation Commission.

This Organization Committee will come to an end as soon as may be after the Railway Company has been constituted, the Railway Commissioner appointed and this plan has been put into operation. The expenses of the Committee and of their staff shall be an operating charge upon the receipts of the German railways.

Article X

ARBITRATION

The law to be enacted by the German Parliament shall provide that so long as the functions of the Railway Commissioner hereinbefore mentioned shall not have come to an end, if any dispute or difference should arise between

the Reparation Commission or any Government represented thereon, on the one side, and the Company and the German Government, or either of them, on the other side, or between the Company and the German Government, as to the interpretation of any provision of the said law, or of the charter of the Company, or of this plan, or as to anything to be done under any of them respectively, whether in respect of the capital and obligations of the Company or of its external, or internal management, or otherwise howsoever, the same shall be referred to the decision of an arbitrator who, if the German Government so desires, shall be of neutral nationality to be nominated by the President for the time being of the Permanent Court of International Justice, and the decision of the arbitrator so appointed shall be final.

ANNEX NO. 5 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

PLAN FOR INDUSTRIAL DEBENTURES

THE AMOUNT AND FORM

1. The German Government shall provide bonds or debentures of industrial concerns to a total nominal value of five (5) milliards of gold marks, bearing five per cent (5%) interest and one per cent (1%) for sinking fund per annum. These bonds shall be the individual obligations of the several concerns and shall be secured as to principal, interest, and sinking fund payments by a first mortgage on the plant and property of the respective concerns making them.

The term "industrial concerns" shall include not only manufacturing concerns, but navigation, mining and any other similar concerns which the Organization Committee may indicate.

DELIVERY TO TRUSTEE

II. The mortgage bonds or debentures above provided for, with suitable coupons covering the interest payments, shall be delivered by the German Government to the Trustee to be appointed by the Reparation Commission, who will hold them, collect the coupons thereon, paying the proceeds into the account of the Agent for reparation payments, or dispose of them in whole or in part from time to time under the orders of the Reparation Commission. The debtor may make proposals to the Trustee for their immediate or gradual redemption, and the Committee recom-

mends that the Trustee be empowered to give preference to such proposals of redemption and especially those of which the redemption would be effected by the use of foreign currencies, before offering such bonds in the open market or otherwise. In the event that no proposals of a satisfactory plan of redemption are made to the Trustee by any individual maker of the bonds within six months after such bonds shall have been delivered to him by the German Government, then the Trustee in his discretion, but with due regard to the protection of the credit of the debtor shall be free to dispose of the same in such manner and on such terms as the Reparation Commission may authorize.

GUARANTEE BY GERMAN GOVERNMENT

III. The German Government shall guarantee the principal, interest and sinking fund payments on such bonds; in consequence, in case of default the matured coupons can be presented to the Commissioner of Controlled Revenues, who shall purchase them at their nominal value, by means of the funds under his control which are destined to be paid over to the German Government. The Commissioner will include the coupons for their nominal value in the "reversements" to the German Government, which will have recourse against the defaulting debtor.

The German Government might, by means of subsidies, encourage the re-purchase of the bonds by the mortgagors and thus free itself from its guarantee.

TAX-EXEMPTION PROVISION

IV. The said bonds and mortgages until redeemed shall be exempt from taxation in Germany, unless they shall be held by German nationals, in which case they shall be taxed like other similar bonds and mortgages so held by German nationals and without discrimination.

TEMPORARY ORGANIZATION COMMITTEE

V. A temporary Organization Committee shall be formed for the purpose of taking all necessary measures within the scope of the foregoing plan and for fixing the details of organization. This Committee shall include a representative of the German Government, a representative of industry, two members appointed by the Reparation Commission and a fifth member of neutral nationality to be chosen by the four thus appointed, or in default of such choice to be appointed by the Reparation Commission.

POWERS OF THE ORGANIZATION COMMITTEE

VI. A. The Organization Committee shall have all powers to work out the details of the plan in such form as may be fair alike to the German Government, to the industrial concerns and to the Reparation Commission, bearing in mind that it is the purpose and intent of the plan to ensure for reparations account the payment of the 5 milliards of gold marks with interest thereon at 5% per annum and a sinking fund of not less than 1% thereon, which in and of itself will determine the maturity of the bonds.

B. The Organization Committee shall have the power to determine the form and character of the mortgages, and, in case the concerns are too small to make individual mortgage issues practical and desirable, the Committee shall have power to devise some method of handling them, or may waive them altogether, provided the total sum of 5 milliards is maintained.

ANNEX NO. 6 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

THE TRANSFER OF REPARATION PAYMENTS FROM GERMAN CURRENCY INTO FOREIGN CURRENCY AND THE USE OF BALANCES NOT TRANSFERRED

TRANSFER COMMITTEE

I. The plan provides that all payments for the account of reparations, however derived, are to be first made in the form of deposits in the bank, provided for in the plan, to the credit of "The agent for reparation payments." The withdrawals from this deposit shall be made by the agent for reparation payments only, under the direction of a committee composed of five members known as "the transfer committee."

COMPOSITION AND SELECTION OF MEMBERS

II. The transfer committee shall be composed of six members; the agent for reparation payments shall be a member and the chairman; the other five members shall be persons qualified to deal with foreign-exchange questions. They shall consist of an American member, a French member, an English member, an Italian member, and a Belgian member. Each of them shall be appointed by the Reparation Commission, after the member of the general board of the bank of the same nationality has been consulted.

COOPERATION OF THE BANK

III. The committee will be in contact with the president and the commissioner of the bank.

POWERS OF THE COMMITTEE

IV. The committee shall have power, and it shall be its duty: *(a)* To apply such bank balances for payments for deliveries in kind and payments under the reparation recovery act, in accordance with the program established periodically by the Reparation Commission, after consultation with the transfer committee as to the character and amount of such deliveries.

(b) To convert these bank balances into foreign currencies from time to time and after conversion to remit them in accordance with the instructions of the Reparation Commission.

Both the foregoing powers *(a)* and *(b)* to be exercised to the extent to which, in the judgment of the committee, the foreign exchange market will permit, without threatening the stability of the German currency.

(c) To invest from time to time in bonds or other loans in Germany such amounts as the committee may deem wise. The committee shall proceed to make these investments as soon as the amount of the credits exceeds the sum which the bank will keep on deposit. On the other hand, the committee may sell the bonds which it has acquired or liquidate the loans which it has granted whenever in its opinion the sums may be converted into foreign exchange, or the bank can accept additional deposits.

RESTRICTION ON PURCHASE BY THE CREDITORS

V. The goods supplied by Germany to the creditor countries under paragraph IV *(a)* above and paid for by

the bank as above provided shall be for the sole use of the countries receiving them for their internal requirements, including the requirements of their colonies and dependencies. The goods so delivered shall not be exported from the country receiving them, except by agreement between the committee acting unanimously and the German Government.

VI. In addition to its powers under paragraph IV, the committee may, on the instructions of the Reparation Commission and at the request of the creditor states, by debiting their accounts, transfer marks to private individuals for the purpose of making purchases in Germany, such reinvestment not to be of a temporary character, and such property being of classes contained in a schedule agreed to between the committee and the German Government and modified from time to time by similar agreement. In arriving at such agreement the German Government shall be required to have due regard to the necessity for making maximum payments to its creditors, but it shall also be entitled to have regard to maintaining its control of its own internal economy.

COOPERATION BY THE GERMAN GOVERNMENT AND THE BANK

VII. The German Government and the bank shall undertake to facilitate in every reasonable way within their power the work of the committee in making transfers of funds, including such steps as will aid in the control of foreign exchange. When the committee is of the opinion that the bank's discount rate is not in relation to the necessity of making important transfers, it shall inform the president of the bank.

ATTEMPTS TO DEFEAT TRANSFER

VIII. In the event of concerted financial maneuvers either by the Government or by any group, for the purpose of preventing such transfers, the committee may take

such action as may be necessary to defeat such maneuvers; and in such circumstances it may suspend the operation of paragraph X, may accumulate the funds or employ them in the purchase of any kind of property in Germany.

TAX-EXEMPTION PROVISION

IX. The German Government shall not tax the deposits in the bank or goods purchased for the creditor countries pending removal, nor any securities or loans representing investment of funds pending transfer, nor any property purchased under the provisions of the paragraph next preceding. This exemption does not apply to property purchased under paragraph VI, but on the other hand, there should be no tax discrimination against such property.

PROVISIONS FOR LIMITATION OF ACCUMULATION

X. *(a)* When the accumulation of funds not transferable under the provisions of subdivisions *(b)* and *(c)* of paragraph IV shall have reached the sum of 5 milliard gold marks (whether represented by bank deposits or loans), the payment for treaty charges provided for shall be reduced to such an amount as will cover the transfers and payments provided for under subdivision *(b)* and *(c)* of paragraph IV without additional accumulation. Such partial suspense of Germany's obligations shall be operative only during the period that the conditions of transfer necessitate, and the standards of payment laid down in the plan shall be resumed at any time when they can operate without the limits of accumulation herein laid down being exceeded.

(b) The committee shall have power to suspend accumulation before reaching 5 milliard gold marks, if two-thirds of its members are of the opinion that such accumu-

lation is a menace to the fiscal or economic situation in Germany or to the interests of the creditor countries.

(c) The committee shall, by a two-third majority, have power to waive the limit accumulations under the conditions provided for in paragraph VIII.

ANNEX NO. 7 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

NOTE OF THE CURRENCIES CIRCULATING IN GERMANY IN JANUARY, 1924 *

Chapter I.—Paper-Mark Currency

A. LEGAL TENDER

1. *Reichsmarks.*—Reichsmarks are issued by the Reichsbank under a pivilege granted to it by the banking law of March 14, 1875. In 1913 the circulation of paper marks amounted to 2.1 milliard; on January 31, 1924, it had reached the figure of 483.7 trillion (English) paper marks, representing 483.7 million gold marks at the rate of 1 gold mark=1 billion paper marks.

2. *Notes of private banks.*—Banks, which at the time of the promulgation of the law of March 14, 1875, had the right to issue notes, have retained this privilege. The number of these banks, which was originally 32, has decreased progressively; at the present time there are only four private banks, namely: Bayerische Banken, Sachsiche Bank, Badische Bank, Wurtembergische Notenbank.

The total circulation of notes issued by these four institutions amounted in 1913 to 140,000,000 gold marks. At the end of January, 1924, it represented about 100,000 gold marks.

3. *Reichskassenscheine.*—These currency notes were issued at the time of the formation of the Reichsbank

* In the English text of this document the English system of enumeration is followed throughout.

(1875) in order to make it possible to place the fiduciary circulation on a sound basis by means of the withdrawal of the State notes then in circulation. The issue was originally fixed at 120,000,000 gold marks, corresponding exactly to the war treasure (in gold) deposited at Spandau. The circulation, which reached the figure of 320,000,000 in 1920 progressively decreased until August, 1923, when it still amounted to 200,000,000 gold marks. At that date the Reichskassenscheine in circulation were completely withdrawn.

4. *Darlehenskassenscheine.*—(Bonds issued by the Darlehenskassen during the war.) The issue reached its maximum figure in October, 1922 (14 milliard paper marks); these bonds ceased to figure in the statements as from August, 1923, when the circulation amounted to only 11 milliard paper marks, corresponding to less than 10,000 gold marks.

B. AUXILIARY INSTRUMENTS OF PAYMENT

1. *Issue of secured notgeld.*—The issue of notgeld (emergency currency) was regulated by the law of July 17, 1922. This currency was issued with a view to supplementing that issued by the Reich, the Reichsbank, and the private banks of issue, the total value of which in circulation was constantly decreasing as a result of the fall of the mark. The previous authorization of the minister of finance was necessary. The notgeld was to be secured by a deposit in fixed values, earmarked in favor of the Reich Minister of Finance, and corresponding to the amount placed in circulation, less the actual or estimated expenses of issue. This asset was to remain at the Reichskreditanstalt at Berlin, which would allow interest at 2 per cent less than the rate of discount of the Reichsbank. The cover for the notgeld might also consist of three

months treasury bonds; but in this case it was the Reichsbank which would issue the notgeld and accept the deposit in treasury bonds offered as guarantee.

Authorization to issue notgeld was granted to public and private organizations for a total figure which at the end of 1923 amounted to 7.6 trillion paper marks, corresponding to 7.6 million gold marks. The circulation of this notgeld amounted on December 31, 1923, to 3.4 trillion paper marks; that is, 3.4 million gold marks. An endeavor has since been made to withdraw the notgeld from circulation; a decree of January 2, 1924, prescribed the complete withdrawal in certain unoccupied territories. On January 31, 1924, the circulation amounted to 1.4 trillion paper marks, or 1.4 million gold marks.

2. *Issue of unsecured notgeld.*—Numerous emergency currencies have been issued without authorization from the German Government, and without the formation of a guarantee deposit, both by public and private organizations and even by private individuals.

The amount of this notgeld issued without authorization or guarantee and in circulation at the end of January, 1924, is estimated by the German Government as follows:

	Gold marks
In unoccupied territory	27,600,000
In occupied territory	132,000,000

3. *Railway notgeld.*—In order to cover the working deficit, the Reich railways issued 114 trillion paper marks during 1922 and 1923. This currency was secured by a Reich deposit at the Reichsbank of 90,000,000 rentenmarks. At the end of January, 1924, 56,000,000 were still in circulation.

Chapter II.—Instruments of Payment in Gold or at a Fixed Value

1. *Rentenmark.*—The rentenbank was created by the decree of October 15, 1923. The method of creation and operation is known.

The issue of notes in rentenmarks began on November 15, 1923.

According to the balance sheet of the rentenbank on January 31, 1923, the amount issued at that date was 1,374,000,000 rentenmarks.

The introduction of the rentenmark has stopped the issue of notgeld of fixed value.

2. *Dollar treasury bonds (Dollarschatzanweisungen).*—The law of March 2, 1923, authorized the issue of dollar treasury bonds for a total amount of $50,000,000 (210,000,000 gold marks). These bonds, issued in denominations of from $5 to $100, do not bear interest, but are redeemable in gold at 120 per cent on April 15, 1926.

These treasury bonds have been fully subscribed. They have been used in Germany as a means of payment.

3. *Gold loan (Wertbestandige Anleihe).*—This loan authorized by the law of August 14, 1923, is for a total sum of 500,000,000 gold marks, which has been fully subscribed. The bonds are expressed in dollars. The small denominations of from one-tenth to $5 do not bear interest and are redeemable at 170 per cent on September 2, 1935. Bonds for $10 or more bear 6 per cent interest and are redeemable at par on the same date. These large denominations were issued first for a total sum of 164,000,000 gold marks. Subsequent issues of large denominations raised this figure to 204,000,000 gold marks.

In October, 1923, the monetary situation having become intolerable on account of the fall of the paper mark, and wage earners having insisted upon being paid in currency

of fixed value, the Reich decided (the preparations for the issue of the rentenmark not being sufficiently advanced) to issue small denominations of the gold loan.

These small denominations were issued up to a total amount of 296,000,000 gold marks, 4,000,000 of which were exchanged against rentenmarks in January, 1924, in accordance with the privilege granted to the holders in this respect.

As will be seen later, 10,000,000 of this gold loan have been assigned as partial security for the notgeld of a fixed value issued by the railways.

At the end of January, 1924, therefore, the circulation was as follows:

	Gold marks
Large notes	194,000,000
Small notes	292,000,000
Total	486,000,000

4.—*Notgeld secured by 6 per cent treasury bonds (6 per cent Schatzanweisungen).*—Since the small gold loan certificates proved insufficient for the monetary circulation, the Provinces, towns, chambers of commerce, and the larger industrial undertakings were given authority to create emergency currency on a gold mark basis, to be covered by gold loan certificates of large denominations. Owing to the scarcity of the latter, the authorities issuing notgeld were given permission to provide cover in the form of 6 per cent treasury bonds expressed in dollars and gold marks, specially created for this purpose by the decree of October 20, 1923. These bonds fall due on December 1, 1932, and are redeemable at par in German currency on a gold basis.

The total amount of notgeld thus secured (exclusive of the notgeld issued by the railways and to which we will

refer later) stood at 110,000,000 gold marks on January 31, 1924.

This notgeld is to be gradually withdrawn from circulation against redemption in loan bonds or German currency. Redemption was to begin on January 15, 1924, and it is hoped that the full amount will have been called in not later than April 1, 1924.

5. *Treasury bonds and interim bonds issued by the States.*—Certain States issued fixed value loans, some of the certificates for which were of such small denominations that they still serve as instruments of payment. The total value of these bonds amounts to about 50,000,000 gold marks. Attempts are being made to recall these small denominations by converting them into larger denominations.

6. *Certificates issued by the banks of Hamburg and Schleswig-Holstein.*—Two banks, the Hamburger Bank von 1923 A. G. and the Schleswig-Holsteinische Goldgirobank A. G., were authorized by the Reich Minister of Finance to deliver, in exchange for currencies, "discount certificates" (Verrechnungsscheine), which still serve as instruments of payment. It is the intention of the German Government to dispense with these gold certificates as soon as a gold currency has been reinstated. The Hamburger Bank issued certificates to the amount of 25,000,000 gold marks. No particulars are available regarding the amount issued by the Schleswig-Holsteinische Goldgirobank, but the figure is inconsiderable.

7. *Notgeld issued by the railways.*—In order to cover their deficit, the German railways were authorized to issue, in addition to the paper mark notgeld referred to above, notgeld having stable value to the amount of 200,000,000 gold marks—10,000,000 of this issue were secured by gold loan bonds, as explained above, the remaining 190,000,000 being secured by 6 per cent treasury bonds, as already

stated. The notgeld issued by the railways amounted to 131,900,000 on January 31, 1924. This emergency currency is to be withdrawn from circulation by means of a loan to be issued later by the railways.

TABLE OF INSTRUMENTS OF PAYMENT IN CIRCULATION IN GERMANY IN JANUARY, 1924

	Approximate value in millions of gold marks *	
I. Instruments of payment expressed in paper marks:		
Reichsbank notes (as per return dated 31/1/24).....	483.7	
Notes of the four private banks of issue	0.1	
Notgeld issued by the railways and secured by a deposit of 90,000,000 rentenmarks at the Reichbank	56.0	
Notgeld issued against the deposit of security in currencies	1.4	
Notgeld issued without cover—		
In occupied territory.....	132.0	
In unoccupied territory..	27.6	
Total		700.8
II. Instruments of payment expressed in gold or having fixed value:		
Rentenmarks (as per rentenbank return of 31/1/24)..	1,374.0	

* Calculated on the basis of 1 gold mark=1 billion paper marks.

	Approximate value in millions of gold marks	
Dollar treasury bonds (Dollarschatzanweisungen, law of March 2, 1923)	210.0	
Gold loan (Wertbestandige Anleihe, law of August 14, 1923)	486.0	
Notgeld secured by 6 per cent treasury bonds (6 per cent Schatzanweisungen, law of October 20, 1923)	110.0	
Treasury bonds and interim bonds issued by the States	50.0	
Certificates issued by the banks of Hamburg and Schleswig-Holstein (Verrechnungsscheine)	35.0	
Notgeld issued by the railways and secured by 6 per cent treasury bonds (10,000,000 of which are secured by gold loan)	131.9	
Total		2,396.9
III. Denominational currency in rentenpfennigs		158.0
Grand total		3.255.7

NOTE.—This total does not include the foreign currencies at present in Germany, which, according to the estimate made by the Second Committee of Experts, would amount to 1,200,000,000 gold marks, a figure which has been confirmed by a German authoritative source.

ANNEX NO. 8 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

Provisional Survey of the Budget for 1924 *

I. GENERAL ADMINISTRATION OF THE REICH

A. Ordinary Budget

Revenue	In millions of—			Expenditure	In millions of—		
	Gold m'ks	£	Dollars		Gold m'ks	£	Dollars
1. Taxes on property, traffic, trade and transfer (direct taxes)...	4,004	200.2	1,001.0	1. Interest on, and amortis, of debt of Empire	156	7.8	39.0
2. Custom and excise duties (indirect taxes)	1,080	54.0	270.0	2. Provision for invalids, war pensions, etc.	810	40.5	202.5
3. Nontax revenues from public services	60	3.0	15.0	3. Army and Navy.....	450	22.5	112.5
				4. Police	208	10.4	52.0
				5. Industrial and cultural purposes	28	1.4	7.0
				6. Unemployment benefit	500	25.0	125.0
				7. Social and other expenditure...	360	18.0	90.0
				8. Finance and taxation departments	380	19.0	95.0
				9. General administrative expenses other than the above.....	250	12.5	62.5
				10 Assignments to the States and communes	1,800	90.0	450.0
Total of ordinary revenues..	5,144	257.2	1,286.0	Total of ordinary expenditure	4,942	247.1	1,235.5
				B. Extraordinary Budget			
1. Revenue from the mint.....	90	4.5	22.5	1. For war damages and removal of effects of the war.....	6	0.3	1.5
2. Other revenues	40	2.0	10.0	2. Public buildings	44	2.2	11.0
				3. Settlement of war expenditure..	20	1.0	5.0
				4. Settlement of expenditure for the Ruhr	60	3.0	15.0
Total extraordinary revenues	130	6.5	32.5	Total of extraordinary expenditure	130	6.5	32.5
Total of A and B.....	5,274	263.7	1,318.5	Total of A and B.....	5,072	253.6	1,268.0

II. EXECUTION OF THE TREATY OF VERSAILLES			
1. Cash reparation payments..... (Discharge of debt due to the Reichsbank for redemption of an exchequer bill given to Belgium.)	52	2.6	13.0
2. Clearing office payments.....	6	0.3	1.5
3. Cost of armies of occupation...	360	18.0	90.0
4. Rhineland commission	34	1.7	8.5
5. Other interallied commissions including reparation commission	18	0.9	4.5
6. Restitution, substitutions, and dismantlement costs	10	0.5	2.5
7. Home expenditure incurred by the carrying out of the Treaty of Versailles	160	8.0	40.0
Total of expenditure.....	640	32.0	160.0
BALANCE			
I. General administration of the Reich.....	5,072	253.6	1,268.0
II. Execution of the treaty of Versailles.....	640	32.0	160.0
Total of expenditure	5,712	285.6	1,428.0
Revenues	5,274	263.7	1,318.5
Deficit	438	21.9	109.5

* The figures of this table can only serve as a preliminary estimate and are given with all reserve. This estimate of the revenues assumes complete restoration of economic unity between occupied and unoccupied territory, renewed administrative and fiscal supremacy in occupied territory on the part of the Reich and the component States, that the taxes to be levied according to the general laws of the Reich and the States are once more directed into their treasuries.

ANNEX NO. 9 TO THE REPORT OF THE FIRST COMMITTEE OF EXPERTS

COMPARATIVE POSITION OF DIFFERENT INCOMES DRAWN FROM DIVIDENDS IN THE YEARS 1920-21, 1923-24, AND 1924-25

Question Submitted to the German Government by the First Committee of Experts

Assume four men with incomes in gold marks: 15,000, 100,000, 500,000, 1,000,000; *(a)* wholly from dividends of German industrial companies; *(b)* one-half from German and one-half from foreign companies. What amount of income tax (or its substitutes) plus capital tax will be payable on the scales for 1920-21, 1923-24, 1924-25, respectively?

Reply of the German Government

For the following reasons it is impossible to make reliable estimates of the kind desired:

1. Because the fiscal burden for 1920-21 can not be calculated owing to the influence of the depreciation of the currency.

2. Because no assessment exists for 1923 based on sliding scale rates for that year; indeed for 1923 prepayments and payments of balance were collected which were regularly calculated on a coefficient of the 1922 taxes and were therefore not entirely immune from the influence of the depreciation of the currency.

3. Because no income tax levied on a sliding scale

exists so far for 1924; the prepayments for 1924 are collected more according to external standards; the actual income for 1924 will not be assessed until 1925, when it will be based upon a tariff which will be determined by law in the course of the year 1924.

Particulars concerning the form of the taxes will be found in the memorandum transmitted (see for 1920-21: English text, pages 81, 96; French text, pages 81-97; for 1923-24: English text, pages 83-84, 96; French text, pages 84, 97). Reference should be made to the statement concerning the budget estimates of the wages tax and the prepayments on the income and corporation taxes for 1924 transmitted as V *(a)* II 1480, of February 16, 1924.

It should further be pointed out that income from dividends to the amount mentioned existed in Germany before the war to a limited extent only and is unlikely to be found after 1922, owing to economic developments during the period of depreciation of the currency.

As early as 1920, there were only six taxpayers in Germany who had an income from investments of from 3,000,000 to 10,000,000 paper marks, that is, from 200,000 to 667,000 gold marks and 66 with an income from investments of from 1,000,000 to 3,000,000 paper marks, that is, about 67,000 to 200,000 gold marks. From about the middle of 1922 income from investments had practically disappeared.

In view of the circumstances mentioned above, any estimates are attended with exceptional difficulties. An attempt is made below to employ available bases for valuation as required in the questionnaire.

The estimates given in the inclosed table showing the charge on incomes from dividends of 50,000, 100,000, 500,000, and 1,000,000 gold marks fulfill the conditions set forth in the questionnaire—

(a) That the whole income is drawn from dividends of German Industrial companies.

(b) That half the income is drawn from German and half from foreign industrial companies.

It was necessary, in drawing up this table, to include in the calculation of the charges on income derived from dividends of German industrial companies, the taxes which had to be paid by the German companies if they distributed dividends to the amounts in question; it must not be forgotten that this tax is deducted before the distribution of the dividends. In converting the income in gold into paper marks and the taxes in paper marks into gold marks, the rate of the dollar has been used as the basis. This was possible because the income is indicated in gold, and therefore the calculation of the tax at the dollar rate affords a basis for comparison.

In making the calculation the following assumptions have been made:

I. *For 1920-21.*—The dividend has been paid to the taxpayer in 1920. The tax paid by the company has first been deducted from the profits which the company made in 1919 and on which it paid the tax in 1920. A further prior charge consists of the 10 per cent tax on revenue from capital which was deducted from the German dividends of the taxpayer at the time of their receipt in 1920 and which he paid in 1921 for his foreign dividends. From the remaining revenue, after deduction of the tax on revenue from capital, the taxpayer has paid his income tax for 1920 according to schedule. In estimating the actual fiscal burden, account has been taken of the fact that the income was obtained in the year 1920; that the corporation tax and the tax on revenue from capital were paid at the time of receiving the dividends, that is also in 1920, and that on the other hand the tax on revenue from capital in respect of foreign dividends and the income tax were not paid until 1921, and were therefore paid in a depreciated currency. On the basis of the average dollar

rate, one gold mark was in 1920 equivalent to 15 paper marks and in 1921 to 24.9 paper marks.

Example 1.—Let us assume the income from dividends in German companies in 1920 to be 50,000 gold marks =750,000 paper marks. Before distributing 750,000 paper marks, a company in 1920 had to pay an average tax of 127,500 paper marks. The 750,000 paper marks due to the person receiving dividend were, upon receipt, reduced by 10 per cent; that is, by 75,000 paper marks. In 1920, therefore, 202,500 paper marks were paid in taxes= 13,500 gold marks. From the remaining 675,000 paper marks he had to pay the sum of 356,600 paper marks in income tax=14,321 gold marks in 1921. The total charge was therefore 27,821 gold marks.

Example 2.—Let us assume the income from dividends in German companies in 1920 to be 25,000 gold marks = 375,000 paper marks and from foreign companies 25,000 gold marks, making a total of 50,000 gold marks = 750,000 paper marks. Before distributing 375,000 paper marks, German companies had, in 1920, to pay an average tax of 63,750 paper marks = 4,250 gold marks. The 375,000 paper marks in German dividends due to the recipient were, upon receipt, reduced by 10 per cent; that is, by 37,500 paper marks = 2,500 gold marks.

In 1920, therefore, 6,750 gold marks were paid in taxes. In 1921 the person drawing dividends had in the first place to pay a 10 per cent tax on revenue from capital on the 375,000 paper marks; that is, 37,500 paper marks = 1,506 gold marks. Furthermore, after deduction of the tax on revenue from capital he had to pay on the remaining 675,000 paper marks an income tax of 356,600 paper marks = 14,321 gold marks. In this case the 1921 taxes thus amount to 15,827 gold marks. Including the 1920 taxes the total charge is therefore 22,577 gold marks.

II. *For 1923-24.*—It is assumed that the dividends for

1923 have been distributed to the shareholders. In the total prior charge the tax on fortunes has not been taken into account. Only the corporation tax which under the law of March 20, 1923, on the depreciation of currency, was paid by the company for the business year 1922, which year was taken as the basis for the distribution of dividends, has been indicated as the prior charge. On the basis of the tariff the prior charge amounted to 45 per cent. Owing, however, to the great depreciation of currency in 1923, the gold value on the date of payment was insignificant. The prior charge has been indicated therefore at only 3 per cent, since the dollar rate at the time of the payment of the tax, that is on April 25, amounted to 29,200, namely about fifteen times the average dollar rate for 1922 (1,885.78). In many cases, owing to delay in closing the taxes the prior charge was, as a result of the rapid depreciation of currency, much less than 3 per cent. In the case of the person receiving dividends, the tax indicated is that which he had to pay as increased prepayments and payment of balance for 1923.

Since there was no proper assessment for income tax on a sliding scale for 1923, the payments of balance for 1923 have been determined according to the taxpayer's capacity to pay on the basis of his gold mark payments in 1923, and in certain cases on the basis of a lavish expenditure.

If, on the basis of the material at its disposal the finance office can assume that the taxpayer had a gold mark income of 50,000 or 100,000 marks, a charge of at least 25 per cent may be allowed for.

If there are really cases of still higher incomes, a charge of 35 per cent on 500,000 gold marks and of 40 per cent on 1,000,000 gold marks will be paid. The total charge therefore amounts to 28 per cent in the case of incomes of 50,000 and 100,000 gold marks derived from dividends paid by German companies; if half of the income

is derived from foreign companies half of the prior charge constituted by the corporation tax does not come into consideration and the total charge therefore amounts to 26½ per cent. For incomes of 500,000 gold marks the total charge represents 38 per cent or 36½ per cent, for 1,000,000 gold marks 43 per cent or 41½ per cent.

III. *For 1924-25.*—It is assumed that the dividend for 1924 is distributed to the shareholders. The prior charge indicated is the tax which the company has paid as corporation tax prepayments and payment of balance for 1923.

The example of 50,000 gold marks has been calculated as follows—1 gold mark was 449 paper marks, according to the average rates of exchange of the dollar for 1922; 50,000 gold marks therefore equal 22,450,000 paper marks.

First prepayment (under the currency depreciation law of March 20, 1923) 20 per cent = 4,490,000 paper marks, paid on May 25 (1 gold mark = 12,190 paper marks) =369 gold marks.

Second prepayment (under the law for increases of July 9-August 11, 1923), 600×10 per cent=1,347,000,000 paper marks, paid on August 25 (value of the gold mark = 1,120,000) = 1,203 gold marks.

Payment of balance on January 10, 1924 (under article I, section 2, of the second fiscal emergency decree), 0.60 gold mark on each 1,000 marks of the 1922 fiscal debt; the 1922 fiscal debt in respect of dividends amounted to 45 per cent of the sum of 22,450,000 paper marks indicated above; that is, to 10,102,500 paper marks. Consequently, the final payment of 0.6 per thousand in gold = 6,061 gold marks. The total prior charge, therefore, amounts to 7,633 gold marks.

In the case of the person receiving the dividend the only payments demanded are those to be paid as income-tax prepayments and as tax on fortunes in 1924. Ten per cent only is first deducted at the source from the revenue

from investments as income-tax prepayment; this is, therefore 5,000 gold marks on 50,000 gold marks. For the tax on fortunes it is assumed that the dividends paid by German companies average 1 per cent of the quoted value; even this computation must, however, be too high for a great many German companies at the present time.

In the case of foreign companies it is assumed that the dividends amount to 5 per cent of the quoted value of the share; 50,000 marks in dividends from German companies, therefore, represent a quoted value of 5,000,000 marks.

For the shareholders' payments in respect of the tax on fortunes this is valued at only half the quoted value—that is, 2,500,000 marks—since the company itself has to pay a tax on fortunes for which the fortune is assumed to be at least the total quoted value of the shares.

On a total fortune of 2,500,000 marks the tax on fortunes amounts to 17,500 marks. The provisional charge on an income of 50,000 marks from dividends from German companies is therefore as follows:

	Gold marks
Tax on corporations	7,633
Deduction at the source from revenue from investments	5,000
Tax on fortunes	17,500
Total	30,133

If half the dividends come from a foreign company, the charge in respect of the tax on capital is as follows:

Twenty-five thousand marks from German companies. Quoted value 2,500,000 (1 per cent interest), half of which is counted; that is, 1,250,000 marks.

Twenty-five marks from foreign companies. Quoted value 500,000 marks (5 per cent interest) counted in full, since the company does not pay the tax on fortunes in Germany.

The quoted value used for the tax on fortunes is therefore 1,750,000 marks and the sum paid in respect of the tax 11,375 marks.

As half of the dividends come from foreign companies, the deduction at the source on half the revenue from investments in this case also provisionally does not come into consideration. The finance office is, however, entitled to collect prepayments from the taxpayer with due consideration to his requirements. No sum is, however, included in the inclosed table on this account; for, as explained above, the calculations for 1924-25 constitute only provisional tax payments, which represent prepayments on the definite income tax for 1924. For the 1924 income, the taxpayer will still be assessed at the beginning of 1925, and he will then have to make considerable postpayments, which are correspondingly higher in the case of income from foreign dividends from which no deduction at the source has been made in Germany. No sum could be included for postpayments, as the necessary regulations must first be enacted by law during the course of 1924 (in particular the rates of taxation.)

Income in gold marks	Definitive charge		Charge in respect of corporation tax and tax on fortunes; nonrecurrent charge in respect of income tax prepayments, 1924-25
	Corporation tax, tax on revenue from capital, income tax, 1920-21	Corporation tax, income tax, 1923-24	
50,000 [1]	27,821	14,000	30,133
50,000 [2]	22,577	13,250	17,691
100,000 [1]	57,586	28,000	60,266
100,000 [2]	47,098	26,500	37,133
500,000 [1]	295,707	190,000	313,830
500,000 [2]	243,267	182,500	194,415
1,000,000 [1]	593,357	430,000	627,660
1,000,000 [2]	488,477	415,000	388,830

[1] German companies.
[2] Half from German and half from foreign companies.

REPORT OF THE SECOND COMMITTEE OF EXPERTS

Covering Letter

Dear Mr. Chairman: I have the honor to present the unanimous report of the committee appointed by the Reparation Commission to inquire into the amount of German exported capital and to consider the means of bringing it back to Germany.

In laying before you the result of our labors may I be permitted in the name of the committee to express the hope that our work may assist in solving the problems involved in the execution of the treaty of peace.

I remain, yours faithfully.

R. McKenna.

The Chairman, *Reparation Commission.*

Text of the Report

In pursuance of a decision of the Reparation Commission of the 30th of November, 1923, we were created a committee to consider the means of estimating the amount of German exported capital and of bringing it back to Germany. We were convened in Paris on the 21st of January, 1924, and we have held together 38 meetings, first in Paris, then in Berlin, and finally again in Paris. We have examined numerous witnesses and have availed ourselves of the services of trained economists, technical advisers and expert accountants. We have also studied the published works on the subject by well-known economists, and each member of the committee has furnished reports on particular problems.

Our estimates relate to the 31st of December, 1923. Later events may, of course, have either increased or decreased the amount of German capital abroad.

In our investigation of the amount of capital owned by Germans in foreign countries, we were confronted by very considerable difficulties. There are many ways by which Germans can acquire capital abroad, but in most cases no precise figures can be given. It is nearly always a matter of estimate, and the utmost we could hope to do with any degree of certainty was to lay down limits between which the actual amount is to be found. The distance which divides these limits marks the want of precision of the material at our disposal.

One method of investigation, to institute an inquiry through bankers and business men in those countries in which German capital is believed to be deposited or invested, was rejected by us at the outset. We have availed ourselves of all information of a public or official character supplied from countries outside Germany, but we were of opinion that it would be neither proper nor useful to request the disclosure of specific transactions which in general would have been entered into under an implied condition of secrecy. Moreover, we felt that even though all obtainable information were freely given to us, it must be extremely defective, as much German capital in foreign countries is certain in existing circumstances to be hidden in various ways under assumed names.

The method we have adopted is altogether different. Our first step was to form an estimate of the total value of German capital abroad at the outbreak of war.

Next we considered what was the net reduction in this total at the time of the Armistice. We took into account on one side the balance of trade, advances by Germany to her Allies, loss by seizure and sequestration of property confirmed by the Versailles Treaty and loss through depre-

ciation of the value of property and securities. On the other side we considered the sales of German securities, the sales of gold, the accumulation of interest, and finally the effect on the trade balance of the imports into Germany from occupied territories. These imports were commodities either requisitioned without payment, or paid for, in the case of Belgium and Poland, largely by marks which remained in the country, and, in Rumania and occupied France, as well as in Belgium and Poland, by local currencies which the German Government caused to be printed and issued for the purpose.

Finally, starting from the basis of the remaining prewar German assets, we examined in detail the various means by which Germans can have increased or diminished their capital abroad during the period from the Armistice to the close of the year 1923. The reliability of our final estimate depends upon the completeness of our examination of the different elements which make up the total of German foreign acquisitions and of the various ways in which such acquisitions may have been expended.

The chief method by which Germans have acquired foreign assets since the Armistice has been by the sale of mark bank balances. Our estimate of the total sum under this head has been obtained by a procedure founded upon the principle that every foreign sale by a German of a mark bank balance creates at the moment of sale a corresponding holding of a foreign bank balance in Germany. The periodic totals of foreign balances shown in the books of the German banks were disclosed to us, and with the assistance of expert accountants we have been able to ascertain the net proceeds expressed in gold derived from the sale of marks. It is interesting to note that the foreign assets acquired in this way amounted to between seven and eight milliards of gold marks, the whole of which in consequence of the final devaluation of the

mark was lost by more than one million foreigners who at one time or another were buyers of mark credits.

This figure is one of the credit factors in estimating the final total.

Other principal sources of German foreign assets have been the sale of goods, securities, real estate, precious metals and mark bank notes; interest accumulations, tourist expenditure in Germany, German holdings in ceded territories in Poland, Dantzig, etc., foreign money expended by the Allied armies of occupation, remittances from Germans abroad, earnings of shipping, railway and canal freights for foreign goods in transit through Germany, insurance profits, etc.

On the other hand, German foreign assets have been expended on the purchase of goods imported, cash payments to the Allies, interest paid on German securities held abroad, German tourist expenditure, etc.

On all these heads of receipt and expenditure, the German statistical records and estimates, official data, bankers, and business reports, and other similar evidence, have been subjected by us to the most critical scrutiny, and their reliability has been tested by our examination of witnesses and inspection of original sources of information. Our investigations and the evidence obtained led us to discard entirely the values of German imports and exports as stated in the official reports, and to revalue all commodities on the basis of the then current world prices with such allowances as the special circumstances of German trade at the time may have rendered necessary.

After a close examination of all the factors which make up the total sum, we are of opinion that German capital abroad of every kind, including capital of varying degrees of liquidity and capital invested in participations in foreign companies and firms, and after taking into account all credit and debit items, was at the end of the year 1923

not less than 5.7 milliard gold marks and not more than 7.8 milliard gold marks, and we think that the middle figure of 6¾ milliard gold marks is the approximate total.

We draw special attention to the foreign currency in Germany, which, though not included in our valuation of capital held abroad, is so closely akin to a foreign asset that it must not be overlooked. It may indeed be said that this currency, the total of which we estimate at not less than 1 milliard two hundred million gold marks, is a German holding in the most liquid form for conversion into foreign assets.

On the other hand, on a broad view of German financial capacity, the value of the property in Germany held by foreigners should not be left out of account. The annual yield from this property, whether in the form of rent, interest, or dividends, is at present inconsiderable and may at any time become subject to special taxation, particularly in the case of rent in respect of real estate purchased at the low prices current in recent years. We estimate, after very close study of the question, that the real estate and securities owned in Germany by foreigners represent a value of from 1 to 1½ milliard gold marks.

The committee have thought it desirable to give in an annex to this report additional information in respect of their estimates of German assets abroad in 1914 as well as of the principal credit and debit factors, both during and since the war, that have gone to make up the final total of German capital abroad.

The second part of our inquiry was to investigate the means of bringing exported capital back to Germany.

The so-called flight of capital in this instance was in the main the result of the usual factors. It arose principally from the failure of the Government to bring its budget into proper relation, and, as a corrollary of such failure, from the raising of large loans and the direct issue

of paper money. Secondly, it was due to the action of speculators and timid investors who sold their marks against the currency of other countries, while the exporters of goods retained abroad all that was possible of the proceeds of their sales. In the particular case under inquiry, however, the flight of capital was accentuated by the attitude of the people of Germany toward payments to her war creditors and was marked by new and ingenious devices and schemes for evading restrictive legislation and for cloaking the real ownership of foreign balances.

The failure of the methods employed, both old and new, demonstrates the final ineffectiveness of restrictive legislation when successful evasion is so richly rewarded. Neither legal enactment nor severe penalties resulted in disclosure of assets abroad or hampered the flight of capital. We feel that this would have been true whether the Government had or had not used its best endeavors to enforce the laws and regulations.

In our opinion the only way to prevent the exodus of capital from Germany and to encourage its return is to eradicate the cause of the outward movement. Inflation must be permanently stopped. If the issue of currency is strictly confined within the true limits of national requirements on a stable basis of value, the German with capital abroad will feel assured that he will suffer no loss in bringing it home; the speculator can no longer look for a profit from the sale of marks. We have already seen in the case of Austria how, when the currency is fairly stabilized, the necessities of foreign trade tend to bring back existing foreign balances. Restrictive legislation, which in the main has proved futile in preventing the export of capital, becomes superfluous the moment there is no longer any inducement to evade the law. It is indeed to be feared the laws purporting to compel the return of capital would have the reverse effect to that which might be wished.

The method of securing a currency in Germany capable of maintaining a sufficiently stable international value covers the whole question of budgetary equilibrium and the establishment of a bank of issue on a sound basis. These matters, which fall outside the scope of our inquiry, have been referred by the Reparation Commission to another committee whose conclusions we have the advantage of knowing. If effect is given to their recommendations, we think that a considerable part of the German assets now in foreign countries will return in the ordinary course of trade.

While we are of opinion that special legislation to prevent the export of capital or compel its return is not required when a country's finance is on a stable basis, we recognize that in the case of Germany a period of transition must necessarily ensue before stability can be obtained and confidence restored. We suggest that during this period an amnesty should be granted for a limited time from the penalties imposed by existing enactments and that special terms be offered for subscriptions to Government loans made in foreign currencies. Well-conceived measures of this kind would be helpful in hastening the return of capital and the final restoration of financial equilibrium in Germany, conditions which are essential to the payment of reparation.

We desire to express our sincere thanks to the officers of the Reparation Commission, and to the economists, statisticians, and expert accountants who have aided us, for whose valuable assistance we are greatly indebted.

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APRIL 9, 1924.

ANNEX

Summary

I. Assets abroad in 1914.

II. Period of the war:
- *a.* Surplus of imports and Germany's advances to her Allies.
- *b.* Depreciation of pre-war foreign assets; sequestration and liquidation measures;
- *c.* Profits realized by Germany in occupied territories;
- *d.* Sale of gold and German securities;
- *e.* Return from German assets abroad.

III. Post-war period:
- *a.* Surplus of imports and cash payments made by Germany under the Peace Treaty;
- *b.* Sales to foreigners of mark credits and bank-notes;
- *c.* Sales of gold.
- *d.* Sales of German real property and German securities;
- *e.* Expenditure by foreigners traveling in Germany and by Germans traveling abroad;
- *f.* Expenditures by the armies of occupation;
- *g.* Earnings from shipping, insurance, transit, etc.;
- *h.* Income from German investments abroad and from foreign investments in Germany; remittances made by Germans residing abroad;

i. German private property in ceded territories;
j. Foreign bank notes in Germany.

I. Assets Abroad in 1914

The value of German assets abroad in 1914 has been estimated by different economists at sums varying between 20 and 35 milliard gold marks. Besides these unofficial estimates two estimates of an official nature, as well as a census, have been made by the German Government. The earlier of these two official estimates is that made in 1905 by the imperial admiralty; the later one was supplied by the German Government in 1924 in reply to a question raised by the second Committee of Experts. The census, which only covered securities, was made by the German Government during the war, in August, 1916.

In the question put to the German Government the committee not only asked for an estimate of the foreign assets held by German nationals in 1914, but also requested it to submit its comments on the various estimates already made by German economists.

All these documents—estimates of German economists, and those of neutral, allied and associated countries, official estimates and census, and the replies of the German Government—have been examined and compared. Taking into account all the factors of valuation, the committee has come to the conclusion that the figure of 28 milliard gold marks may be accepted as representing the value of German assets abroad at the time of the declaration of war, it being understood that this figure of 28 milliards comprises only the assets abroad belonging to German nationals residing in Germany and not those belonging to German nationals residing abroad. In this estimate securities have been taken at their face value in gold marks.

II. Period of the War

(a) Surplus of imports and Germany's advances to her allies

The difficulty encountered by Germany in exporting her goods during the war, as well as her persistent endeavors to increase her imports by every possible means, in order to provide for the requirements of her armies, naturally produced a surplus of imports, considerably in excess of the figures of the normal pre-war deficit. To this deficit in Germany's foreign trade balance must be added the sums advanced by Germany to her allies to enable them to pay for their imports, for which she received no corresponding return. The figure indicated for these two items may be considered to be reliable and amounts to an aggregate sum of 15.2 milliard gold marks, subject to the modifications referred to in paragraph *(c)*.

(b) Depreciation of pre-war foreign assets; sequestration and liquidation measures

Various estimates of the reduction in German assets abroad during the war as a result of depreciation have been made by several economists, whose figures are generally based on an estimated total of from 20 to 25 milliard gold marks for German assets in 1914. Their estimates seem too low, if we take as a basis the figure of 28 milliards adopted by the committee for German assets abroad in 1914. This impression is moreover confirmed by information which the committee has obtained by its own investigation.

It is impossible to adopt a definite figure in determining the value of the assets seized and liquidated in the allied and associated countries. On the basis of information obtained by the committee from the Government of

the allied and associated powers as well as from Germany, the committee has been able to estimate at approximately 16.1 milliard gold marks the reduction in German assets abroad during the war, as a result of depreciation and liquidation and sequestration measures. In adopting this figure no allowance has been made for the fact that certain German assets abroad may have been utilized to cover the payment of imports, nor for the fact that German assets abroad may have increased owing to the accumulation of the interest accruing on these assets. These several items are discussed elsewhere. The above figure therefore represents a net reduction in German assets abroad for which Germany during the war period received no return. These assets underwent a further decrease in value during the period following hostilities, which decrease was taken into account.

Lastly, the committee is of opinion that both during and since the war, the category of assets in neutral countries has likewise undergone a reduction in value, and that in particular the greater part of such securities held by Germans has no longer a value equivalent to their face value, even taking into account the effect of the decline in the value of gold.

(c) PROFITS REALIZED BY GERMANY IN OCCUPIED TERRITORIES

An examination of German economic measures taken in Belgium during the war, to which the attention of the committee was called, suggested that substantial profits had accrued to Germany from the exploitation of occupied territories. Consequently the committee has made a careful study covering not only German operations in Belgium and northern France but also those in Poland and Rumania.

No attention has been paid to the purely military aspects of these operations, such as, for instance, requisi-

tions intended to provide for the partial subsistence of the German occupying troops. Quite apart from such matters, however, it was found that the profits realized by Germany by requisitions and by other methods in occupied territories are closely connected with the deficit of the German balance of trade. With the help of German official documents, in particular reports by the military administration drawn up during the war and German memoranda estimating the value of war damages, the committee has ascertained that the profits realized by Germany were principally obtained as follows:

Germany obtained in occupied territories considerable quantities of commodities which, through the operation of centralized importing companies specially created for this purpose were transported to Germany for internal consumption. Most of these goods were either not paid for at all, or were paid for in paper marks which were subsequently left in the country and amounted in the case of Belgium to 6 milliard paper marks, or were purchased through the medium of issues of local paper currency. The special object of such issues, according to a statement by the German staff, was to enable Germany and her allies to receive goods from occupied territories free of charge during the whole period of hostilities.

By requisition or in exchange for paper marks or local currency Germany also obtained considerable quantities of the currency of invaded countries. Thus, in the north of France the German military authorities imposed on towns fines and levies for which payment was required in German money, gold coin, or notes of the Bank of France.

Finally, foreign assets were required by Germany, especially in Belgium and France, notably by means of sequestration of securities, coupons, and other credits, and these, like the bank notes mentioned above, served in part to pay for imports from neighboring neutral countries.

It must also be pointed out that when the German coal centrale in Belgium issued export licenses for coal for Holland, Switzerland, or Sweden, the German authority kept for itself the foreign currency thus obtained, and forced the mines to accept paper marks.

The committee has adopted the figure of from 5.7 to 6 milliard gold marks as corresponding to that portion of the profits derived from this exploitation of Belgium, northern France, Poland, Lithuania, Rumania, etc., representing imports for which no payment was made and which, in consequence, had not been allowed for in her balance of accounts.

(d) SALE OF GOLD AND GERMAN SECURITIES

The sale of gold and securities was the principal means whereby Germany paid for her imports during the war. The export of gold, which took place mainly during the early years of the war, reached a total amount of 1 milliard gold marks.

As regards German securities, widely diverging estimates have been made of the amounts sold. In our opinion the total figure is not far from 1 milliard gold marks.

(e) RETURN FROM GERMAN ASSETS ABROAD

The revenue which Germany derived from her assets abroad was very considerably diminished immediately after the declaration of war and further reductions occurred during the period of hostilities.

It should, indeed, be noted that interest ceased to be paid on the assets held by Germany in countries with which she was at war. Some of these assets were sold during the war and the depreciation of others became very marked toward the end.

On the other hand, the industrial securities, particu-

larly those of neutral countries, continued to pay interest at rates frequently higher than before the war.

While the committee has been unable to determine exactly the variations for each year of the war in the revenue derived from German assets abroad, it has at least been able to make an estimate which may be taken as very nearly accurate.

III. Post-war Period

(a) Surplus of imports and cash payments made by Germany under the peace treaty

One of the main causes of the reduction of German assets abroad during the post-war period arose from the necessity for Germany to cover the deficit in her trade balance and to meet the cash payments which had to be made to the Allies under the Treaty of Versailles. These two items together amount to between 9 and 10 milliard gold marks.

As already stated in the report the figures given in the official German foreign trade statistics are quite inaccurate for certain periods. This observation applies particularly to the figures originally published.

For this reason, it was necessary to revise completely the balance given for every year. Taking into account the various factors entering into the calculation, the committee is of opinion that this revision has made it possible to reach a figure more nearly equal to the actual excess of imports than had been the case in previous reports dealing with this question. The fixing of the amount of the deficit in the trade balance is of true importance, since any valuation that is to be made of German assets remaining abroad largely depends on the figure finally adopted for that deficit.

The cash payments made by Germany to the Allies—to

the Reparation Commission, under the reparation recovery act, payments to the clearing office, etc.—do not give rise to dispute.

(b) SALE TO FOREIGNERS OF MARK CREDITS AND BANK NOTES

Germany has acquired foreign assets in large volume since the armistice through opening credit accounts in her banks for the benefit of foreigners. These credits were paid for by the foreigners in the money or credits of other countries, and as they underwent a constant shrinkage in real value through the depreciating value of the mark, German economy profited largely from the transactions. The committee made a careful study of the values so acquired by an investigation, with the aid of expert accountants, of the mark credit balances on foreign account in the principal banks of Germany during the post-war years.

It was found that there had been during this five-year period more than a million individual accounts of this kind. In most cases the mark credits of these accounts had not been immediately utilized and had undergone a process of shrinkage through the depreciation of mark values that amounted to a veritable evaporation.

The work of the expert accountants was directed to determine as nearly as possible the aggregate amount of the shrinkages in these very numerous accounts that was due to the depreciation of the value of the mark. With this end in view the leading banks in Germany were asked to transcribe from their books the data showing the credit balances and the amounts of debits in the accounts of all foreigners at the close of each month from the end of 1918 to the end of 1923.

After the sums indicated had been converted to gold equivalents at the current rate of exchange, it was possible to draw close inferences as to the total gains accruing to

German economy as a whole. The data furnished by the banks were submitted to careful checking by the expert accountants, and it was found that they had been correctly compiled.

Credits in German marks were purchased by the citizens of a great many nations, but the largest amounts were taken by the citizens of a relatively restricted group of countries.

The methods used in determining the value of the assets acquired by the German banks in this way were subjected to an interesting check which consisted of taking a single account of a foreigner who had engaged in speculative operations on a considerable scale, and converting the figures of the transactions to a gold basis for every day on which any debit or credit entry was recorded. The results indicated that there was no tendency for this detailed method of conversion to yield results materially different from those found by the more general mass methods that it was necessary to employ in computing the figures for Germany as a whole.

When the whole inquiry, which was of considerable length, had been completed it was found that Germany had profited by the sale of mark credits by an amount of from 7 to 8 milliards of gold marks. In addition the sale of paper marks in foreign countries had resulted in profits amounting to from 600 to 700 millions of gold marks, or a total from these two sources of 7.6 to 8.7 milliards of gold marks.

(c) SALES OF GOLD

German official statistics record sales abroad by Germany principally in the years 1919-1921 and 1923 of gold to a total amount of 1½ milliard gold marks. The accuracy of these figures is not disputed.

(d) SALES OF GERMAN REAL PROPERTY AND GERMAN SECURITIES

During the period characterized by the rapid depreciation of the mark, sales of real property to foreigners reached an unwonted development in Germany.

In estimating the proceeds of such sales, the committee had before it various statistics indicating in detail the number and amount of sales of real property to foreigners since the war in some of the principal towns of Germany, and also in districts of varying economic character.

As regards securities, Germany was able during the first part of the post-war period to market some of her securities abroad, but as soon as her financial position became more uncertain most of these transactions were suspended.

In the aggregate the committee considers that sales of German real property and securities to foreigners amounted to about 1½ milliard gold marks.

(e) EXPENDITURE BY FOREIGNERS TRAVELING IN GERMANY AND BY GERMANS TRAVELING ABROAD

During the five years which have elapsed since the Armistice, considerable sums have been spent in Germany by large numbers of foreigners who have traveled and lived in the country. Our estimate of the expenditure by these travelers was facilitated by the official statistics kept by the largest German towns and by the German Government. The committee was able to obtain a fairly exact idea of the number of foreigners who came to Germany during the period in question, the average length of their stay and the daily expenditure of each traveler.

As against this, numerous German travelers belonging mostly to the wealthier classes have stayed in foreign countries, especially in the last two or three years. Their

expenditure has to be deducted from the expenditure by foreigners in Germany referred to above, and very considerably reduces the amount of the German assets realized from that source.

(f) EXPENDITURE BY ARMIES OF OCCUPATION

During the post-war period, a certain sum has been realized by Germany through the expenditure in foreign currency, or in marks bought with foreign currency, by the troops occupying German territory.

Each of the Governments having or having had armies of occupation in Germany has supplied the committee with a detailed estimate of the expenditure made by the officers and men or by the various army services. These estimates were checked in several ways by a series of calculations relating to each army's different methods. The results of these different calculations have been combined.

(g) EARNINGS FROM SHIPPING, INSURANCE, TRANSIT, ETC.

Earnings from shipping, insurance, commissions, transit, were an important source of German income prior to 1914, but during the war such earnings in great measure disappeared. In the five years 1919-1923 some of the lost ground has been regained, particularly in the field of shipping and insurance, and the committee has taken this item into account.

(h) INCOME FROM GERMAN INVESTMENTS ABROAD AND FOREIGN INVESTMENTS IN GERMANY—REMITTANCES MADE BY GERMANS RESIDING ABROAD

The total amount of the income produced by German assets abroad since 1919 is of course substantially below that produced by German assets abroad before the war. The assets held abroad by Germany since the war repre-

sent indeed only a small and for some part unproductive fraction of her pre-war holdings. It is true, on the other hand, that the payments which Germany has had to make since 1919 in respect of German securities held by foreigners have been inconsiderable. After a careful study of the question, the committee came to the conclusion that a set-off of the two items—income from German investments abroad and income from foreign investments in Germany—resulted in a small balance in Germany's favor for the whole of the post-war period.

The remittances sent to Germany by German nationals residing abroad and German connections and sympathizers amount to a considerable figure in Germany's favor.

(i) GERMAN PRIVATE PROPERTY IN CEDED TERRITORIES

Most of the valuations of German property abroad have taken little or no account of the value of German private property in the ceded territories of Silesia, Posen, Danzig, etc.

These properties are included in our own estimate in so far as, according to the definition adopted by the committee, they are owned by Germans residing in Germany. Although it is very difficult to determine with any precision the extent of these properties, the committee considered that it should not exclude from its valuation certain industrial assets, particularly those in Upper Silesia.

(j) FOREIGN BANK NOTES IN GERMANY

There is in Germany a large quantity of foreign bank notes (dollars, florins, Scandinavian crowns, Swiss francs, pounds sterling, and more especially in the occupied territory, Belgian and French francs). The exceptional plight of the German mark has influenced Germans in acquiring

stable currencies wherever possible and on a large scale. These foreign notes have remained in the country instead of finding their way abroad again through the normal channel of trade, as would have been the case in ordinary circumstances.

Various estimates of the total amount of such notes were made in Germany, particularly toward the end of 1923. The committee has compared the different estimates with the information which it collected in Germany and other countries. In its opinion, the value of the foreign notes existing in Germany at the end of 1923 amounted to about 1.2 milliard gold marks.

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